LIBRARY
SUPREME COURT, U.S.

Supreme Court, U.S.
FILED
JUN 25 1971
E. ROBERT SEAVER, CLERK

No. ~~1880~~

70-334

In the

Supreme Court of the United States

OCTOBER TERM, 1971

DU PAGE UTILITY COMPANY,

Petitioner,

vs.

ILLINOIS COMMERCE COMMISSION,

Respondent.

PETITION FOR A WRIT OF CERTIORARI TO THE SUPREME COURT OF ILLINOIS

JOHN N. VANDER VRIES
and
DANIEL J. KUCERA
111 West Monroe Street
Chicago, Illinois 60603
Attorneys for Petitioner

The Scheffer Press, Inc.—ANdover 3-6850

INDEX

	PAGE
Opinion Below	1
Jurisdiction	2
Questions Presented	2
Statement of the Case	3
Nature of Operations	3
Reasons for Proposed Rate Increase	3
Hearings and Rehearing	4
Commission's Order on Rehearing	4
Valuation of Plant	4
Return under Rates Proposed by Du Page	5
Commission's Finding of Rate Base and Allowed Return	5
Manner in Which Federal Questions Raised	8
Reasons for Granting Writ	11
I. The Decisions Below are Contrary to the Requirements of the Fourteenth Amendment and Decisions of the United States Supreme Court that a Public Utility is Entitled to Rates Providing Just Compensation	11
II. The Decisions Below Conflict with Decisions of the United States Supreme Court and of the Highest Courts of Other States that the Source of Money Used by a Utility to Construct Its Plant Has No Bearing Upon Constitutional Protection Against Confiscatory Rates	15

PAGE

III. The Decisions Below Completely Disregard the Value of Du Page's Plant and Thereby Violate the Fourteenth Amendment and the Prior Decisions of This Court and of the Illinois Supreme Court that a Public Utility is Entitled to a Reasonable Return Upon the Present Fair Value of Its Property 17

IV. The Decisions Below Affect Every Public Utility in Illinois; Raise Important Questions Faced by Utilities and Regulators in Every State; and Conflict With Decisions in Other States That Follow the New York Telephone Case 22

A. The Decisions Below Affect Every Public Utility Company in Illinois 22

B. The Decisions Below Raise Significant and Recurring Questions Faced by Public Utilities in Every State 23

C. The Decisions Below Conflict with Those in Other States as to Constitutional Protections 23

V. The Decisions Below Patently Violate Due Process Because They Hold that Purchasers of Improved Lots from a Development Company Which has Common Ownership with a Utility Company by Imputation Pay For Utility Plant .. 24

Conclusion 28

Appendix 1a

Order of Illinois Commerce Commission 1a

Application for Rehearing 9a

Order on Rehearing of Commission 15a

Application for Rehearing 40a

PAGE

Opinion of Circuit Court for the Eighteenth Judicial Circuit 53a

Order of Circuit Court 60a

Opinion of Supreme Court of Illinois 61a

Petition for Rehearing 70a

Order Denying Rehearing 81a

CITATIONS

CASES:

Arizona Corporation Commission v. *Arizona Water Co.*, 335 P. 2d 412 (1959) 16

Bluefield Waterworks and Improvement Company v. *Public Service Commission*, 262 U.S. 679 (1923) 11, 18

Board of Public Utility Commissioners v. *New York Telephone Company*, 271 U.S. 23 (1926) 11, 15, 25

City of Chicago v. *Commerce Commission*, 4 Ill. 2d 554, 123 NE 2d 500 (1955) 20

City of Edwardsville v. *Bell Tel. Co.*, 310 Ill. 618, 142 NE 197 (1923) 14

Federal Power Commission v. *Hope Natural Gas Company*, 320 U.S. 591 (1944) 12, 19

Federal Power Commission v. *Natural Gas Pipeline Co.*, 315 U.S. 575 (1942) 18

Federal Power Commission v. *United Gas Pipe Line Co.*, 386 U.S. 237 (1967) 20

Illinois Bell Telephone Co. v. *Commerce Commission*, 414 Ill. 275, 111 NE 2d 329 (1953) 20

Killarney Water Co. v. *Commerce Commission*, 37 Ill. 2d 345, 226 NE 2d 858 (1967) 22

McCardle v. *Indianapolis Water Co.*, 272 U.S. 400 (1926) 21

PAGE

New Rochelle Water Co. v. *Maltbie*, 289 NYS 388 (1936) 15

Peoples Natural Gas Co. v. *Pennsylvania Public Utility Commission*, 34 A 2d 375 (1943) 15, 16

Preston Utilities Corp. v. *Commerce Commission*, 39 Ill. 2d 457, 236 NE 2d 714 (1968) 22

Public Util. Com'n v. *Springfield Gas Co.*, 291 Ill. 209, 125 NE 891 (1920) 12, 18

Smyth v. *Ames*, 169 U.S. 466 (1898) 17

STATUTES:

Ill. Rev. Stat. c. 111⅔, sec. 36, 41 ..... 12, 18

IN THE

SUPREME COURT OF THE UNITED STATES

OCTOBER TERM, 1971

No.

DU PAGE UTILITY COMPANY,

Petitioner,

vs.

ILLINOIS COMMERCE COMMISSION,

Respondent.

PETITION FOR A WRIT OF CERTIORARI TO THE SUPREME COURT OF ILLINOIS

The petitioner Du Page Utility Company respectfully prays that a writ of certiorari issue to review the judgment and opinion of the Supreme Court of Illinois entered in this proceeding on January 25, 1971.

OPINION BELOW

The opinion of the Supreme Court of Illinois is reported at 47 Ill. 2d 550, 267 N.E. 2d 662, and also appears in the Appendix hereto. The opinion of the Circuit Court for the Eighteenth Judicial Circuit, Du Page County, Illinois, and the rate order on rehearing of the Illinois Commerce Commission are unreported, but appear in the Appendix hereto.

JURISDICTION

The opinion and judgment of the Supreme Court of Illinois was entered January 25, 1971. A timely petition for rehearing was denied on March 31, 1971, and a copy of the order of denial appears in the Appendix hereto. This petition for certiorari was filed within 90 days of said denial of rehearing. This Court's jurisdiction is invoked under 28 U.S.C. §1257(3).

QUESTIONS PRESENTED

1. Whether the decisions below violate the Fourteenth Amendment requirement that a public utility is entitled to rates providing just compensation, by their denial of rates sufficient to yield a reasonable return, and thereby are confiscatory of utility property?

2. Whether the decisions below violate the Fourteenth Amendment requirement that the source of money used by a utility to construct its plant has no bearing upon Constitutional protection against confiscatory rates?

3. Whether the decisions below, by their deduction from rate base of purported contributions in aid of construction in an amount exceeding the value of utility plant, and by allowing no return whatsoever on property of admitted substantial value violate the Fourteenth Amendment?

4. Whether the decisions below violate the Fourteenth Amendment requirement that a public utility is entitled to a reasonable return on the present fair value of its property?

5. Because Illinois is a "fair value" state, whether the decisions below violate due process by their disregard of the criteria of fair value rate base established by prior decisions of this Court and the Supreme Court of Illinois?

6. Whether the decisions below violate due process by imputing that customers made contributions in aid of construction deductible from rate base merely because they purchased improved lots from a developer or that a developer adopted a particular federal income tax treatment of his donations to the capital of the utility?

7. What Constitutional requirements and protections under the Fourteenth Amendment apply to the public utility rate-making process of state regulatory agencies after the *Hope Natural Gas* case?

STATEMENT OF THE CASE

Nature of Operations

DuPage Utility Company ("DuPage") is a public utility corporation which provides metered water service and sanitary sewerage disposal service to approximately 840 customers, mostly residential, but including some commercial and institutional customers, in Lisle, Illinois and vicinity. DuPage owns a complete interconnected water supply and distribution system, including two wells, an elevated storage tank, and the usual mains, valves, fire hydrants, customer services and meters. The sewerage disposal system consists of the usual collecting mains and appurtenances thereto. Initially, the Company also had a sewage treatment plant. In 1961, this treatment plant was sold to the County of Du Page and since then, all sewage is delivered to the County for treatment and the Company is charged by the County for such sewage treatment service furnished to the Company.

Reasons for Proposed Rate Increase

On February 20, 1967, DuPage filed with the Illinois Commerce Commission new rate schedules proposing revi-

sions in rates for general water service and for general sanitary sewer disposal service (Resp. Ex. 3 and 4, R. Unit II. Vol. 2, Sec. 38). It filed for a rate increase because the existing rates were insufficient to cover operating expenses, with the result that the company had continually lost money and was suffering a negative rate of return. (R. Unit II, Vol. 2, Sec. 32, p. 18-19). DuPage experienced a net operating loss every year since 1962. For the 12 months ended December 31, 1966 (the test year) DuPage suffered a net operating loss of $10,732.65 and had accumulated a total *deficit* of $81,549.38 (Resp. Ex. 8, R. Unit II, Vol. 2, Sec. 38).

Hearings and Rehearing

The Commission suspended the proposed rate increases, and beginning April 24, 1967, held five hearings. The Commission entered an order on January 17, 1968, denying the proposed rates. Both DuPage and intervenors filed separate Applications for Rehearing, which were subsequently granted. Rehearing was held on March 11, 1968, at which time DuPage presented additional testimony and exhibits. On April 16, 1968, the Commission entered its Order on Rehearing, from which DuPage subsequently appealed.

Commission's Order on Rehearing:

Valuation of Plant

The original cost and the reproduction cost new valuations of DuPage's utility plant are not in dispute. The Commission found that the original cost of DuPage's plant, after deducting depreciation, is $788,610.52. (Order on Rehearing, Finding (5), R. Unit II, Vol. 1, Sec. 26). Of this, $476,309.82 is water plant, and $312,300.70 is sewer plant. The Commission also found that the reproduction cost new,

after deducting depreciation, is $888,214.04. Of this, $541,400.56 is water plant, and $346,813.48 is sewer plant.

Return under Rates Proposed by DuPage

The Commission found and DuPage accepts, that if the proposed rates were in effect in the test year, they would produce pro forma net income of $24,769.00. Of this, $23,341.00 would be from the water operations and $1,428 from the sewer operations. (Order on Rehearing, p. 17, R. Unit II, Vol. 1, Sec. 26). This constitutes a return or net original cost of 3.14% and on net reproduction cost new of 2.79%.

Commission's Finding of Rate Base and Allowed Return

Although the Commission found net original cost to be $788,610.52 and net reproduction cost new to be $888,214.04, the Commission fixed a total "fair value" rate base at only $16,555 and allowed a total return to the Company of $1,076. (Appendix A and B, Order on Rehearing, R. Unit II, Vol. 1, Sec. 26). The allowance of $1,076 is a rate of return of 0.136% on the Commission's finding of net original cost and 0.121% on its finding of net reproduction cost new.

In its finding of "fair value" rate base, upon which it bases its calculation of "reasonable return," the Commission eliminated net original cost and net reproduction cost new. It allowed only the item of cash working capital, a non-plant item, as total rate base. In reaching this conclusion, the Commission made total deductions from plant valuation of $814,992.19. This deduction comprised three separate deductions: (1) The Commission reclassified $793,195.25, representing cash donations to capital by affiliated interests of shareholders of DuPage, from capital surplus to

"contributions in aid of construction" and deducted same together with additional donations, for a total of $798,-702.25; (2) It deducted customer's advances for construction in the amount of $15,669.64; and (3) it deducted unamortized investment credit in the amount of $620.30. (Appendix A, Order on Rehearing, R. Unit II, Vol. 1, Sec. 26).

In other words, as Appendix A to the order clearly shows, the $16,555 rate base contains absolutely *no* element of *value*, or allowance for *value* of the physical *plant*. To paraphrase Appendix A:

1.	Net Utility Plant in Service at Original Cost	$788,610.52
2.	Net Utility Plant in Service at Reproduction Cost New	$888,214.04
3.	"Weighted Cost"	$813,511.40
4.	"Deductions"	$814,992.19
5.	"Fair Value of Utility Plant for Rate Base"	-0-
6.	Add: Working Capital Requirements	$16,555.00
7.	"Fair Value Rate Base"	$16,555.00

The Commission found that pro forma net operating expense would be $130,788. However, it then disallowed half of officers' salaries of $31,560. After making adjustments in the federal income tax for this disallowance as well as for reduction of return from $24,769.00 to $1,076, the Commission found DuPage's "revenue requirements" to be $109,240. The Commission concluded that DuPage required additional revenues of $13,729, the difference between $109,240 and actual 1966 revenue of $95,511. Finally, the Commission denied the proposed rate increase, but ordered DuPage to put into effect new rates which the Com-

mission concluded would produce the additional $13,729. (R. Unit II, Vol. 1, Sec. 26.)

The Order on Rehearing contains a dissenting opinion stating, in part:

> "The application of the theories of the Uniform System of Accounts to rate making procedures for water and sewer utilities, has always been, in my opinion, [an] anathema to equity and good conscience.
>
> "The case at bar, is very much in point and demonstrates the futility of our historic treatment of 'contributions in aid of construction.' * * *
>
> "We say in this case that it would cost almost a million dollars to replace this plant and that it cost more than $800,000 to build in the first place and yet, by what I believe to be antiquated and inapplicable accounting procedures this Commission has arrived at the conclusion that $16,555 is a fair value rate base. ***
>
> "In my opinion, we should reject the Uniform System of Accounts in these cases and adopt a formula that is realistic, keeping in mind, that the law of Illinois requires us to arrive at a 'fair value' rate base and that other formulas are inapplicable here."

Du Page filed its Application for Rehearing from the Commission's Order on Rehearing. (R. Unit II, Vol. 1, Sec. 28). On May 29, 1968, the Commission denied Du Page's Application for Rehearing. (R. Unit II, Vol. 1, Sec. 30).

On July 5, 1968, Du Page filed its appeal to the Circuit Court of the Eighteenth Judicial Circuit, Du Page County, which was docketed as No. 68-1511-G (R. Unit I, Sec. 5).

On February 6, 1970, the Court entered its written opinion affirming the Commission's Order on Rehearing (R. Unit I, Sec. 28, c. 99), and on February 24, 1970, it entered its written order in accordance therewith. (R. Unit I, Sec. 22).

In the Circuit Court's written opinion, Judge Guild stated:

> "I cannot help but feel that the amount of return allowed is, in fact, so small that it probably is not financially feasible for the utility company to continue operations."

Du Page subsequently filed its timely appeal to the Supreme Court of Illinois. On January 25, 1971, the Supreme Court of Illinois entered its opinion and judgment, appearing in the Appendix, affirming the Circuit Court and the Commission's rate order. A timely petition for rehearing was denied on March 31, 1971.

Manner in Which Federal Questions Raised

The proceedings before the Illinois Commerce Commission commenced when the Commission suspended the new tariffs filed by Du Page and set the matter for hearing. Accordingly, the first pleading filed by Du Page raising federal questions was an application for rehearing (R. Unit II, Vol. 1, Sec. 23), after the Commission entered its original order on January 19, 1968 denying the new tariffs. In the application for rehearing, Du Page raised the federal questions under the Fourteenth Amendment of confiscation, discrimination, denial of just compensation, denial of reasonable return, and deduction from rate base of alleged contributions and failure to determine rate of return upon present fair value of the Company's utility plant. Relevant portions of the application for rehearing appear in the Appendix hereto. The Commission granted rehearing on February 26, 1968. On April 16, 1968, the Commission entered its order on rehearing again denying the proposed tariffs. (R. Unit II, Vol. 1, Sec. 26) The order contains a dissenting opinion which relates to the federal ques-

tions, and a copy of the order appears in the Appendix hereto. On May 15, 1968, Du Page filed an application for rehearing (R. Unit II, Vol. 1, Sec. 28) raising the above federal questions; a copy appears in the Appendix hereto. Rehearing was denied on May 29, 1968 by a minute order. (R. Unit II, Vol. 1, Sec. 30).

Pursuant to the Illinois Public Utilities Act, Ill. Rev. Stat. c. 111⅔, sec. 1, et seq., Du Page appealed from the order on rehearing and the order denying rehearing thereof on July 5, 1968 to the Circuit Court for the Eighteenth Judicial Circuit, Du Page County. Under Illinois law, review by the Circuit Court is solely on the record before the Commission and the court does accept additional pleadings but does not hold a de novo hearing. The above federal questions were raised and argued both in oral argument and in briefs in the Circuit Court. On February 6, 1970, the Circuit Court affirmed the Commission's order stating in part:

> "I cannot help but feel that the amount of return allowed is, in fact, so small that it probably is not financially feasible for the utility company to continue operations. I am inclined to agree with the dissent of the late Robert Dolph, one of the members of the Commerce Commission. However, I am bound by the [Illinois] Supreme Court decisions and I feel that the cases cited specifically apply to the factual situation here."

A copy of the Circuit Court's opinion appears in the Appendix hereto and at R. Unit I, C.99.

On March 2, 1970, Du Page appealed to the Supreme Court of Illinois. There, both in oral argument and briefs, the same federal questions were raised and argued and were, in fact, focal points of the appeal. On January 25,

1971, the Supreme Court of Illinois entered its order which appears in the Appendix hereto and which affirms the Commission's order on rehearing. On February 15, 1971, Du Page filed a petition for rehearing with the Court against raising these federal questions, which petition appears in the Appendix hereto. On March 31, 1971, the petition was denied without opinion. A copy of said order appears in the Appendix hereto.

REASONS FOR GRANTING WRIT

I. THE DECISIONS BELOW ARE CONTRARY TO THE REQUIREMENTS OF THE FOURTEENTH AMENDMENT AND DECISIONS OF THE UNITED STATES SUPREME COURT THAT A PUBLIC UTILITY IS ENTITLED TO RATES PROVIDING JUST COMPENSATION.

The Commerce Commission permitted Du Page a return after expenses of only $1,076. Du Page serves 840 customers. The Commission found that its utility plant had a net original cost of approximately $800,000 and a net reproduction cost new of approximately $900,000. It also found that Du Page had annual net operating expenses of over $109,000.

In the Circuit Court's written opinion, Judge Guild stated:

> "I cannot help but feel that the amount of return allowed is, in fact, so small that it probably is not financially feasible for the utility company to continue operations."

In rate-making by a state regulatory commission, a public utility company is protected by a constitutional requirement of just compensation. Under the Fourteenth Amendment, just compensation is a reasonable return upon the value of property devoted to public service. Rates not sufficient to yield a reasonable return are confiscatory, and their enforcement deprives a public utility company of its property in violation of the Fourteenth Amendment. *Board of Public Utility Commissioners* v. *New York Telephone Company*, 271 U.S. 23, 31 (1926); *Bluefield Waterworks and Improvement Company* v. *Public Service Commission*, 262 U.S. 679, 690 (1923).

The Illinois Public Utilities Act provides that a utility is entitled to "a *reasonable return* upon the *value* of said public utility's property used and useful in rendering its service to the public." Ill. Rev. Stat. c. 111⅔, sec. 36 (Emphasis added). The Supreme Court of Illinois early held that "ultimately in every case of this character the question to be determined is: What is a fair and reasonable return upon the present value of the property employed in rendering the service to the public?" *Public Utilities Commission* v. *Springfield Gas Co.*, 291 Ill. 209, 234, 125 NE 891, 901 (1920).

Just compensation is a fundamental constitutional protection regardless of the application or interpretation of the decision in *Federal Power Commission* v. *Hope Natural Gas Company*, 320 U.S. 591 (1944). (See Reason III *infra.*) Indeed, in the *Hope* case, this Court held that under the Natural Gas Act, regardless of what formulas are used in rate-making, the end result of a rate order must be just and reasonable. This Court also stated that a utility is entitled to a return "sufficient to assure confidence in the financial integrity of the enterprise, so as to maintain its credit and to attract capital." *Id.* at 603.

It is obvious on the face of the Commission's rate order, which was affirmed by the Supreme Court of Illinois, that the decisions below denied Du Page just compensation and a reasonable return, contrary to the Fourteenth Amendment. Under any rational test, this is confiscation of Du Page's property. The permitted return is a return on net original cost of 0.136% and a return on net reproduction cost new of 0.121%. Accordingly, the return on present fair value is somewhere in the range of 1/10th of 1%. Obviously, this return is not sufficient to insure the financial integrity of the enterprise. It is less than 1% of the Commission's finding of annual net operating expense. If a well

were to fail or a water main to break, who will pay for this additional cost? It is also obvious that the permitted return will not allow Du Page to maintain its credit or attract capital. Interest is not includable in operating expense. Thus, the $1,076 would be the maximum money available for debt interest as well as the only cushion for an unusual operating expense, or for inflation.

In affirming the Commission's rate order, the decision of the Supreme Court of Illinois, regardless of formula, deprives Du Page of all benefits of ownership of property, yet imposes a duty to maintain and operate its plant. In fixing rate base, the Commission made deductions in excess of plant value. It permitted as a rate base only a working capital allowance—a non-plant item calculated as a percentage of operating expense.

With the burden, should come the benefit. The Commission, however, has permitted Du Page only the burden. It has denied Du Page *any return.* Du Page *owns* its plant. It uses this plant to operate a public utility business and to provide public utility service to nearly 1,000 customers. The plant has *value.* It is required to repair, maintain, and improve the plant. It must operate the plant. It must provide service. It cannot cease business or close its doors.

Yet—no return. In no other situation has the law denied a legitimate private enterprise the right to earn a return, yet compelled it to continue to operate. The owner forever is deprived of any and all economic benefit whatsoever from ownership. This *is* confiscation.

Neither the U.S. nor Illinois Constitutions and law permit such results anywhere else. For example, a donee of any other property may sell it or rent it for whatever it

can bring on the market place. Even upon acquisition by government through eminent domain, he is constitutionally entitled to receive its full market value. The immediate result is to deprive the utility of all earnings and to, in effect, transfer the economic ownership of the utility property to the customers, who in turn receive free service to the extent they pay no capital costs.

This result is, contrary even to the Illinois Supreme Court's own prior decisions of 50 years' standing. The leading case of *City of Edwardsville* v. *Bell Tel. Co.*, 310 Ill. 618, 142 NE 197 (1923) firmly established that a public utility may not be compelled to operate at a loss and that any action by the regulatory body that imposes a non-compensatory return on a utility is confiscatory and unconstitutional:

> "The State has no power to compel a corporation engaged in operating a public utility to serve the public without a reasonable compensation. The power of the legislation over rates to be charged is not absolute but is limited. It is the power to regulate and not confiscate. It is a legislative power to fix rates, but it is a judicial question whether the rates fixed are such as to deprive the public utility affected of its property without due process of law. The owners of property invested in public utility corporations are entitled to the equal protection of the law which is guaranteed to all, and they are deprived of it and of their property if the rates fixed by law are so low as to prevent the companies from earning any compensation for the use of the property after keeping it in repair and paying the expenses of operation."
>
> *Id.* 310 Ill. at 621, 142 NE at 199.

By affirming the Commission's order, the Supreme Court of Illinois has left Du Page without any reason to be in business, yet compelled to stay in business. Du Page is reduced to the equivalent of a receivership or trustee in

bankruptcy. This is contrary to the Fourteenth Amendment. "The relation between the company and its customers is not of partner, agent and principal or trustee and beneficiary." *Board of Public Utility Commissioners* v. *New York Telephone Company*, 271 U.S. 23, 31 (1926).

This is confiscation.

II. THE DECISIONS BELOW CONFLICT WITH DECISIONS OF THE UNITED STATES SUPREME COURT AND OF THE HIGHEST COURTS OF OTHER STATES THAT THE SOURCE OF MONEY USED BY A UTILITY TO CONSTRUCT ITS PLANT HAS NO BEARING UPON CONSTITUTIONAL PROTECTION AGAINST CONFISCATORY RATES.

When utility plant is devoted to rendering public service, it is included in the rate base regardless of the source of money used by the utility to construct its plant. This constitutional principle was established by the United States Supreme Court in the *New York Telephone* case, where this Court held:

> "Constitutional protection against confiscation does not depend upon the source of the money used to purchase the property. It is enough that it is used to render the service." 271 U.S. at 31.

Several states specifically have followed the *New York Telephone* case. For example, in the leading case of *New Rochelle Water Co.* v. *Maltbie*, 289 NYS 388 (1936), the court held "for rate-making purposes petitioner is entitled to earn a reasonable return upon the value of all property used and useful in providing the service, and the commission had no authority to deduct from such value the sums advanced by consumers for extensions, title to which is in petitioner." *Id.* at 397. In *Peoples Natural Gas Co.* v. *Penn-*

sylvania Public Utility Commission, 34 A 2d 375, 381, (1943), the court stated:

> "That appellant [utility] owns the property and is using it in the service is unquestioned. And, so long as present fair value is the test, it makes no difference whether appellant bought it, received it as a gift, or won it in a lottery."

More recently, the Arizona Supreme Court held to the same effect. *Arizona Corporation Commission* v. *Arizona Water Co.*, 335 P. 2d 412, 415 (1959).

However, the rate order on rehearing of the Illinois Commerce Commission below and the affirming decision of the Illinois Supreme Court below are in direct conflict with these decisions. In purporting to fix a reasonable return on present fair value, the decisions below disregard the doctrine of *New York Telephone*, by adopting the doctrine of deducting from the rate base so-called contributions in aid of construction. After weighing net original cost and net reproduction cost and reaching a weighted cost of $813,511.40 the Commission deducted $814,992.19, finding a so-called "fair value of utility plant" for rate base to be zero or in actuality a negative $1,480.79. The Commission accomplished this by reclassifying shareholder donations to capital into contributions in aid of construction and then deducting the contributions from the rate base.

The Commission's action obviously is contrary to the doctrine of *New York Telephone*. The Illinois Supreme Court upheld its decision on the ground that contributions in aid of construction represent payments for utility plant by customers of the utility. However, it is uncontradicted that all plant of Du Page was constructed and paid by Du Page with its own money. The reclassification into the contributions account was supposedly justified on the

ground that payments by customers could be implied merely from the fact that they had purchased lots which already had existing water and sewer mains in the street.

Whether Du Page received its money from shareholders, affiliates of shareholders, developers, or even directly from customers, should have no bearing upon its right under the Fourteenth Amendment to a reasonable return. Accordingly, the decisions below are in direct conflict with the *New York Telephone* doctrine.

III. THE DECISIONS BELOW COMPLETELY DISREGARD THE VALUE OF DU PAGE'S PLANT AND THEREBY VIOLATE THE FOURTEENTH AMENDMENT AND THE PRIOR DECISIONS OF THIS COURT AND OF THE ILLINOIS SUPREME COURT THAT A PUBLIC UTILITY IS ENTITLED TO A REASONABLE RETURN UPON THE PRESENT FAIR VALUE OF ITS PROPERTY.

Du Page's utility plant has a net original cost of approximately $800,000 and a net reproduction cost new of approximately $900,000. All this plant is used and useful in rendering service to the public. The Commission so found. However, the rate base fixed by the Commission, $16,555, eliminates all value of plant. The decisions below denied Du Page any return on plant having value.

The decision below of the Supreme Court of Illinois by its affirmance of the Commission's rate order rejecting fair value rate base is a total and unprecedented break from both prior decisions of this Court and approximately 60 years of Illinois public utility law. This break is arbitrary, contrary to due process and in conflict with the Fourteenth Amendment of the United States Constitution.

Beginning with *Smyth* v. *Ames*, 169 U.S. 466 (1898), the United States Supreme Court established as a requirement

under the Fourteenth Amendment a present fair value test for rate making by state regulatory authorities: that a utility is entitled to receive a fair and reasonable return on the present fair value of its utility plant used and useful in rendering public service. See *Bluefield Waterworks and Improvement Company* v. *Public Service Commission*, 262 U. S. 679 (1923).

Illinois early adopted this standard. Under the Illinois Public Utilities Act, the Commission is required to fix rates which yield "a reasonable return upon the *value* of said public utility's property used and useful in rendering its service to the public." Ill. Rev. Stat. c. 111⅔, sec. 36, 41. (Emphasis added). Accordingly, the Supreme Court of Illinois held in the leading case of *Public Utilities Commission* v. *Springfield Gas Co.*, 291 Ill. 209, 219, 125 NE 891, 896 (1920) that:

> "The basis of all calculations as to the reasonableness of rates to be charged by a corporation maintaining a public utility under legislative sanction must be the fair value of the property being used by it for the convenience of the public, and in order to ascertain that value the original cost of construction, the amount expended in permanent improvements, the present cost of construction, the probable earning capacity of the property under the particular rates prescribed by statute, and the sum required to meet operating expenses, are all matters for consideration and are to be given such weight as may be just and right in each case."

This holding has been followed and reaffirmed by all subsequent decisions of the Supreme Court of Illinois prior to the decision below.

In the 1940's, the United States Supreme Court rendered two decisions involving rate orders of the Federal Power Commission under the Federal Natural Gas Act. *Federal Power Commission* v. *Natural Gas Pipeline Co.*,

315 U.S. 575 (1942); *Federal Power Commission* v. *Hope Natural Gas Co.*, 320 U.S. 591 (1944). These cases held that the Federal Power Commission was not bound to the use of any single formula or combination of formulae in determining rates. Rather, on review, the question is whether the order, viewed in its entirety, is just and reasonable in the result reached, rather than the method employed in reaching the result.

As we pointed out in Reason I above, this Court's decision in the *Hope* case has no effect upon the Fourteenth Amendment protection to utilities against confiscation and unjust compensation. Furthermore, it is clear that the *Hope* case has no effect upon the Fourteenth Amendment requirement, as established in cases such as *Smyth* v. *Ames* and *Bluefield*, that state regulatory commissions must fix rates which yield a reasonable return upon present fair value rate base.

First, the *Hope* case involves solely a question of rates fixed by the Federal Power Commission under the federal Natural Gas Act. The *Hope* case on its face makes no determination under the Fourteenth Amendment and does not overrule or even discuss rate-making standards applicable to state authorities established in prior cases such as *Smyth* v. *Ames* and *Bluefield*. Accordingly, this Court has never repudiated the present fair value requirement as a constitutional protection under the Fourteenth Amendment and the action of the Commission and the Supreme Court of Illinois in the decisions below must be tested by the doctrine of *Bluefield*.

Second, after the *Hope Natural Gas* decision, Illinois has remained a fair value state and its *Springfield Gas Co.* decision has been followed and reaffirmed by all subsequent decisions of the Illinois Supreme Court until the decisions

below. In *Illinois Bell Telephone Co.* v. *Commerce Commission,* 414 Ill. 275, 287, 111 NE 2d 329, 336 (1953), the Illinois Supreme Court specifically held that the *Hope* case is not a precedent for the formulas adopted by the Illinois Commission. In *City of Chicago* v. *Commerce Commission,* 4 Ill. 2d 554, 558, 123 NE 2d 500, 502 (1955), the court reiterated that a utility must earn a return upon the *present value* of its property. Inasmuch as Illinois remains a present fair value state, the propriety of the Commission's rate orders in terms of the Fourteenth Amendment must be tested by the decisions of the United States Supreme Court prior to *Hope*. The rejection of *Hope* by the Illinois Supreme Court necessarily implies an alignment with the prior United States Supreme Court decisions.

Third, even if this Court should conclude somehow that the *Hope* case altered its prior decisions, this Court nevertheless should test the decisions below, which allegedly were rendered under application of a fair value rate base formula, by standards of due process and fundamental fairness required for application of that formula. As Mr. Justice Harlan, joined by Mr. Justice Douglas and Stewart stated in their dissenting opinion in the recent case of *Federal Power Commission* v. *United Gas Pipe Line Co.,* 386 U.S. 237, 249 n. 3 (1967), notwithstanding the *Hope* "end result" doctrine, there is nothing in *Hope* to suggest that courts should not review a particular formula to determine whether it is based on rational criteria. Inasmuch as Illinois law is "present fair value," this Court should determine whether the decisions below are based on rational criteria consistent with the Fourteenth Amendment, and set out in *Bluefield.*

It is obvious that the decisions below, although giving lip service to fair value in fact fixed a rate base which

makes no allowance for the *value* of Du Page's plant, thereby causing confiscation of its property. Obviously, the Commission could not have determined present fair value of utility plant or given full and fair consideration to net original cost and net reproduction cost, when its order finds value to be zero or negative. In fact, the decisions below wholly disregarded "value" and fixed a rate base having no relationship to fair value or any element of value.

The Commission even denied Du Page any going value, although this Court clearly and repeatedly has held that going value is a *property right,* should be considered in determining value of plant, and upon which the owner has a *right,* to make a fair return. *McCardle* v. *Indianapolis Water Co.*, 272 U.S. 400, 414 (1926).

How can Du Page's physical plant have a zero or negative value? How can plant having an original cost of over $800,000 and a reproduction cost of over $900,000 have a negative fair value? How can a plant which is used in a going-concern business and which renders service to almost 1,000 customers have no value whatsoever, even a going-concern value?

The disregard for value and the elementary unfairness of the Commission's action forces Du Page to do business at a confiscatory net operating loss. The decisions below on their face show a total disregard for the property of Du Page, contrary to the Fourteenth Amendment. As the dissent to the Commission's rate order stated,

> "The fact is, that a plant of value is being used daily by the rate-payers, and granted the event of effective, good service, the rate-payers ought to pay a rate commensurate with the value of the plant they use."

IV. THE DECISIONS BELOW AFFECT EVERY PUBLIC UTILITY IN ILLINOIS; RAISE IMPORTANT QUESTIONS FACED BY UTILITIES AND REGULATORS IN EVERY STATE; AND CONFLICT WITH DECISIONS IN OTHER STATES THAT FOLLOW THE NEW YORK TELEPHONE CASE.

A. THE DECISIONS BELOW AFFECT EVERY PUBLIC UTILITY COMPANY IN ILLINOIS.

The holding of the Supreme Court of Illinois below that contributions in aid of construction should be deducted from plant fair value in determining rate base is an unprecedented break with prior Illinois law. It is the first decision of that Court upholding the deduction of contributions. It is the first decision which disregards the fairness and reasonableness of return allowed a utility. It is the first decision to "impute" contributions in aid (See Reason V). It is the first decision to exclude *value* from rate base.

The decisions below are a culmination of two prior recent decisions of the Illinois Supreme Court, *Killarney Water Co.* v. *Commerce Commission*, 37 Ill. 2d 345, 226 NE 2d 858 (1967); *Preston Utilities Corp.* v. *Commerce Commission*, 39 Ill. 2d 457, 236 NE 2d 714 (1968). *Killarney* was not a rate case but an original cost accounting case. Rates were not involved. The Court upheld the Commission's accounting classification of certain funds as contributions in aid of construction because the land developer affiliated with the water company had specifically segregated a portion of the total proceeds received in the sale of lots and had placed them in segregated water reserve accounts; he never had treated the funds as belonging to him but as funds of the lot purchasers. *Preston*, a rate case, concerned only the original cost element to be considered in determining rate base and merely held that the utility failed to meet

a burden of proof of showing the amount actually spent by the first person to devote the plant to public service.

There are over 100 water companies in Illinois almost all of which carry contributions in aid of construction and many of which were created by a land developer to serve a new subdivision or community. Almost every water company has a portion of its plant contributed in some fashion or other which under the theory of the Supreme Court in Du Page would not be includable in rate base. Many of these companies are identical to Du Page in that the Commission has found them to have for rate-making purposes a minimal or zero rate base.

In addition, various Illinois gas, electric and telephone utilities carry contributions resulting from service extensions.

B. THE DECISIONS BELOW RAISE SIGNIFICANT AND RECURRING QUESTIONS FACED BY PUBLIC UTILITIES IN EVERY STATE.

Du Page Utility Company is not unique to either Illinois or to the nation. In every state having regulatory authorities with jurisdiction over rate-making, the question of contributions in aid of construction is faced, regardless whether the utility is water, sewer, gas, telephone or electric. Practically every utility anywhere carries a contributions account. Practically every utilities commission has adopted a system of accounts similar to that of Illinois.

C. THE DECISIONS BELOW CONFLICT WITH THOSE IN OTHER STATES AS TO CONSTITUTIONAL PROTECTIONS.

As discussed in Reason II, *supra*, several states, including New York, Pennsylvania and Arizona have followed this

Court's decision in the *New York Telephone* case that the source of funds used by a utility to construct its plant has no bearing on rate base. The decisions below, by their deduction of so-called contributions in aid of construction, directly conflict with these decisions.

Accordingly, such conflict raises not only for Illinois, but every state fundamental questions as to what constitutional protections under the Fourteenth Amendment now exist in the state rate making process. More particular, does the *New York Telephone* decision of this Court retain its viability and vitality? Or, are there *no* constitutional requirements, as the Illinois decisions now appear to hold?

V. THE DECISIONS BELOW PATENTLY VIOLATE DUE PROCESS BECAUSE THEY HOLD THAT PURCHASERS OF IMPROVED LOTS FROM A DEVELOPMENT COMPANY WHICH HAS COMMON OWNERSHIP WITH A UTILITY COMPANY BY IMPUTATION PAY FOR UTILITY PLANT.

The decisions below lack fundamental fairness and violate due process because they arbitrarily adopt as controlling two false concepts. First, the decisions below *impute* from the fact that a lot purchaser buys an improved lot that he thereby makes a contribution in aid of construction to a utility, which is deducted from rate base. Second, the decisions below make the federal income tax treatment by a developer on his own books of any moneys he donates to a utility as determinative whether lot purchasers have made contributions in aid of construction to the utility company.

Du Page Utility Company built all its plant with its own money. Most of its cash came from donations to its capital by shareholders or an affiliate of the shareholders. The

affiliate was a development company owned by the utility shareholder. The development company developed the subdivisions which Du Page eventually served. Du Page constructed all subdivision water and sewer lines prior to the sale of lots to individual homeowners. The gist of the Commission's theory, affirmed by the Supreme Court of Illinois, is that when a lot purchaser buys a lot which is adjacent to Du Page's lines he thereby has paid for part of Du Page's plant. Accordingly, the Commission denies Du Page any earnings on that plant.

There is no evidence that any customer of Du Page ever paid even one dollar to Du Page for plant. The most that can be said is that a substantial portion of the cash which Du Page used to pay for its plant came to it from developers. However, certainly this does not mean that this cash was customers' cash. Prior to donations, the developers treated the cash as their funds. It was never segregated. The cash never was traced to lot purhasers. There is no difference here of what occurred and what would have occurred if shareholders had personally given cash to Du Page instead of the development company donating capital. These were capital funds.

The decisions below are contrary to *Board of Public Utility Commissioners* v. *New York Telephone Company*, 271 U.S. 23 (1926). It was argued there that by paying rates for utility service producing revenues in excess of operating expense, customers were paying for the utility plant, and that such plant therefore could not be used to support future rate increases.

This Court rejected this argument with language which is wholly applicable to the Du Page situation.

> "Customers pay for service, not for the property used to render it. Their payments are not contribu-

> tions to depreciation or other operating expenses or to capital to the company. By paying bills for service they do not acquire any interest, legal or equitable, in the property used for their convenience or in the funds of the company. Property paid for out of moneys received for service belongs to the company just as does that purchased out of proceeds of its bonds and stock." *Id.* at 32.

The lot purchaser in the instant case paid for land and not utility plant, just like customers paid for service and not for plant. The money paid the developers belonged to the developers. The lot purchasers lost all title and interest in the money after payment. They certainly acquired no interest, legal or equitable, in the utility plant. If customer does not make a contribution by paying rates to a utility, he certainly does not make one by buying a lot which is already improved by the utility, not the developer, in advance of the purchase.

The decisions below also impute customer contributions because the developer-shareholders "expensed" donations to capital of Du Page for federal income tax purposes.

In arriving at such a result, the Supreme Court of Illinois failed to consider the fact that the homebuilder preparing a complete package for sale also expenses many other items without any similar shift in the economic benefits of property ownership. The homebuilder expenses carpentry, plumbing, electrical and masonry costs for presumably the same tax purpose, but is not required to return to the home purchaser any part of the purchase price equivalent of his so-called tax benefit. He also expenses heavy equipment, automobiles and office buildings, but still retains the full economic benefit of ownership of such items, even though it might be said that he used the home purchasers' money to pay for them if the Court were to

"trace" the dollars in the same manner it does where the *developer* invests in water and sewer improvements. Yet, as a result of the decisions below, he is completely deprived of the economic benefit of one class of property only; i.e., his stock in the utility company.

At any rate, what is this "expensing" of costs? It is merely an accountant's bookkeeping entry. The home-builder who received the purchase price from the purchaser may have used the cash in countless different ways; for example, to pay off a bank loan or to buy more land. The mere accounting entry surely does not establish that the money is traceable into the utility plant.

We also point out that if the developer-stockholder did not "expense" his donations to the capital of Du Page, this would not make the donations any more or any less "customers' funds" under the Commission's theory. How is the lack of "expensing" presumptive evidence that customers did not pay for plant under this argument? There is no showing that the price paid by the home purchaser is affected at all by the tax accounting or bookkeeping of the developer. Rather the record is to the contrary in that the sales price is solely based upon the competitive housing market.

The Commission's order, to paraphrase Cardozo, illustrates the tendency of a "principle" to extend beyond the limits of its logic. Does the theory that the customers paid for Du Page's plant when they purchased their lots apply to a second owner of a house—the transferee of the original lot purchaser? Suppose part of the price of a lot were used by the developer to build houses. Are the lot purchasers entitled to a discount on the purchase of houses because they "paid" for them already?

Do the lot purchasers have an interest in the developer's car or his wife's fur coat? If the developer used the funds to purchase stock of Commonwealth Edison—who also put lines in and serves the subdivision—could he properly keep dividends on the stock? Would the lot purchasers be entitled to discounts on their electric bills? If Du Page financed its plant with a bank loan, but repaid the loan with these funds donated by the shareholders, would there still be a zero rate base? If customers of Commonwealth Edison buy company bonds and the proceeds are used to build a nuclear generating plant, can Edison earn a return on this plant; or was it "paid" for by customers?

The decisions below accordingly deny DuPage due process of law.

CONCLUSION

For these reasons, it is respectfully submitted that the petition for writ of certiorari should be granted to review the judgment and opinion of the Supreme Court of Illinois.

Respectfully Submitted,

JOHN N. VANDER VRIES
DANIEL J. KUCERA
111 West Monroe Street
Chicago, Illinois 60603
Attorneys for Petitioner

APPENDIX

STATE OF ILLINOIS
ILLINOIS COMMERCE COMMISSION

Du Page Utility Company In the matter of the proposed revisions in rates for sewer service, stated in 3rd Revised Sheet No. 1, Ill. C.C. No. 2	53105
Du Page Utility Company In the matter of the proposed revisions in rates for water service, stated in 1st Revised Sheet No. 1, Ill. C.C. No. 1	53106

ORDER

By the Commission:

On February 20, 1967, Du Page Utility Company (hereinafter sometimes referred to as "Respondent") filed with this Commission its rate schedule for sewer service, designated Ill. C.C. No. 2, 3rd Revised Sheet No. 1, and its rate schedule for water service, designated Ill. C.C. No. 1, 1st Revised Sheet No. 1, proposing general increases in sewer and water rates to be effective March 22, 1967.

Notice of the proposed changes was published and posted in accordance with the requirements of law and the provisions of General Order No. 157 of this Commission.

It appeared from an examination thereof that the Commission should enter upon a hearing concerning the pro-

priety and reasonableness of the proposed changes and increases in said rates, and that pending the hearing and the Commission's decision thereon the proposed changes and increases should not become effective. Accordingly, the Commission, by its orders entered on March 8, 1967, suspended the proposed changes and rate increases until July 19, 1967, and thereafter by further orders entered on July 12, 1967, resuspended said proposed changes and rate increases for an additional period until January 19, 1968.

Pursuant to notice duly given, a hearing was held on these matters before a duly authorized Examiner of the Commission at its offices in Chicago, Illinois, on April 24, 1967. At that time, on motion of the Respondent, Ill. C.C. Docket Nos. 53105 and 53106 were consolidated for the purpose of hearing and order. The Respondent appeared by counsel, and presented oral and documentary evidence in support of its proposed changes in rate increases. Applications for leave to intervene and appearances were filed and entered on behalf of the Meadows Community Association, and at a subsequent hearing, on behalf of the Oak View Homeowners Association. Appearances were also entered on behalf of the Accounting and Engineering Staffs of the Commission. There were no other appearances. Further hearings were held on June 6, August 21 and August 30, 1967, and at the conclusion of the hearing on the last date, the consolidated cases were marked "Heard and Taken."

On October 24, 1967, Respondent filed its request in writing for oral argument before the Commission which request was thereafter withdrawn, and on November 29, 1967, the Commission granted Respondent's motion to reopen the hearing for the purpose of presenting new

and additional pertinent evidence. Further hearing was had on December 13, 1967, at the conclusion of which, the matter was again marked "Heard and Taken."

Du Page Utility Company provides water and sewage disposal service to approximately 840 customers consisting mostly of residential customers in the Oak View Subdivision in the Village of Lisle, Illinois, and the Meadows Subdivision immediately south of the Village in Du Page County, Illinois. A few commercial customers are included in a shopping center area and a recreation area known as Four Lakes, also near the Village of Lisle, in Du Page County.

Respondent obtains its water supply from two wells connected to a common distribution system. Initially it owned and operated a sewage treatment plant which was sold to Du Page County in 1961. Respondent now pays Du Page County a specific rate to handle its sewage treatment, which rate is subject to an increase commencing May 1, 1968.

Sewage disposal service is presently rendered by Respondent to single-family residences at a flat rate of $2.50 per month or $7.50 per quarter. The proposed new rate is $4.50 per month or $9.00 per two-month period. Service to multi-family, commercial and institutional users is presently rendered at a rate of $.50 per 1,000 gallons of water used per month as per meter reading or the flat rate presently charged single-family residences, whichever is greater. The proposed schedule continues the 10% delayed payment charge and also provides that any connection charge imposed by the County of Du Page, which furnishes sewage treatment service to the Company, shall be paid by the customer to said County prior to commencement of service.

General metered water service is presently rendered in Lisle and vicinity by the Company under the following rates:

First	3,000 Gals. or less per month or 9,000 Gals. or less per quarter	$.75 per 1,000 Gals.
Next	5,000 Gals. per month or 15,000 Gals. per quarter	$.60 per 1,000 Gals.
Over	8,000 Gals. per month or 24,000 Gals. per quarter	$.45 per 1,000 Gals.

The proposed rates for metered water service are as follows:

First 1,000 Cu. ft. per 2 month period	$.84 per 100 Cu. ft.
Next 1,000 Cu. ft. per 2 month period	$.70 per 100 Cu. ft.
Next 3,000 Cu. ft. per 2 month period	$.56 per 100 Cu. ft.
Over 5,000 Cu. ft. per 2 month period	$.40 per 100 Cu. ft.

The present minimum water bill is $2.25 per month or $6.75 per quarter. The proposed minimum bill per 2 month period is $8.40, for which up to 1,000 cubic feet of water will be allowed without addition charge. Presently, most customers are billed quarterly. The Company proposes to bill most customers per 2 month period, but reserve the right to bill monthly, in which case the rate blocks and minimum bill shall be one-half of those for the 2 month period above stated. The proposed schedule continues the 10% delayed payment charge.

The Company presented oral testimony and documentary evidence of original cost of utility plant for water and sewer service in the aggregate sum of $875,418.55, the aggregated accumulated depreciation in the sum of $87,717.38, reproduction cost new in the sum of $986,322.74 and cash working capital requirements in the sum of

$17,852.00, as of December 31, 1966. On the basis of its evidence presented Respondent claimed that the fair value of its property used and useful in rendering water service and sewage disposal service to the public for rate making purposes is not less than $840,000.

The Objectors presented evidence contending that the sum of $793,195.25 transferred on the books of the Respondent on December 31, 1966, from an account entitled "Contributions in Aid of Construction" to an account entitled "Capital in Excess of Par Value of Shares" was in fact "Contributions in Aid of Construction" and should have been deducted from the utility plant in service to arrive at a proper fair value rate base, and that if this were done the Respondent would have no fair value rate or very little for rate making purposes. The Objectors further contended that the sum of $31,680 paid to the officers of the company who were also the sole shareholders in the company as salaries was excessive for the amount of time and the nature of the services performed by these officers.

The Commission having considered all of the evidence, both oral and documentary, and being fully advised in the premises, is of the opinion and finds that:

(1) Du Page Utility Company is engaged in furnishing water and sewage disposal service in certain areas in the Village of Lisle, Du Page County, Illinois, and vicinity, and is a public utility within the meaning of an Act entitled "An Act concerning public utilities," as amended; the Commission has jurisdiction of the parties and of the subject matter herein;

(2) on February 20, 1967, Du Page Utility Company filed with the Commission its rate schedule Ill. C.C. No. 2, 3rd Revised Sheet No. 1, pro-

posing to increase the rates for sewage disposal service furnished by it, and its rate schedule Ill. C.C. No. 1, First Revised Sheet No. 1, proposing to increase the rates for water service furnished by it;

(3) due notice of the filing of said rate schedules was given pursuant to law and the rules and regulations of the Commission;

(4) on March 8, 1967, the Commission issued its suspension order suspending the proposed water and sewer rates to July 19, 1967, pending hearing, and thereafter, on July 12, 1967, resuspended such proposed rates to January 19, 1968;

(5) there is an original cost proceeding now pending before this Commission with respect to the Respondent's water and sewer plant; and that, for the purpose of this rate case, the original cost of Respondent's water plant and property used and useful in rendering service to the public, as of December 31, 1966, was $528,059.65, and the provision for depreciation was $52,659.18, resulting in a net original cost depreciation as of December 31, 1966, of $475,400.47; the original cost of Respondent's sewage disposal plant used and useful in rendering service to the public as of December 31, 1966, was $347,358.90, and the accumulated provision and depreciation on said net plant was $35,058.20, resulting in a net original cost depreciated for the sewage disposal plant, as of December 31, 1966, of $312,200.70; the total net original cost for both the water and sewage disposal plant and property depreciated as of December 31, 1966, for the purpose of these proceedings was $787,701.17;

(6) the reproduction cost new of the used and useful property of Du Page Utility Company, as

of December 31, 1966, was $986,322.74, which, less an allowance for depreciation of $99,018.05, would result in reproduction cost new less depreciation, as of December 31, 1966, of $887,304.69; that the reproduction cost new, as of December 31, 1966, of Du Page Utility Company's plant and property used and useful in providing water service was $600,545.79, the reserve for depreciation was $60,054.58, and net reproduction cost new was $540,491.21; that the reproduction cost new, as of December 31, 1966, of Du Page Utility Company's plant and property used and useful in providing sewerage disposal service was $385,776.95, the reserve for depreciation was $38,963.47, and net reproduction cost new was $346,813.48;

(7) the salaries of the officers in the sum of $31,680 was excessive and that a more reasonable amount for officers' salaries for the service performed would be ½ that amount or the sum of $15,840; that with the adjustment of officers' salaries the working capital requirements of the Respondent is $15,625.50 for seventy-five (75) days;

(8) the sum of $793,195.25 representing cash contributions from interests affiliated with the shareholders of Respondent constitutes "contributions in aid of construction" and not capital surplus, and that said sum together with additional contributions in aid of construction in the aggregate amount of $798,702.55 should be deducted from the cost of utility plant in service in computing its fair value for rate making purposes;

(9) for the purpose of this proceedinng, the company's fair value rate base was no greater than $13,235.36;

(10) Respondent's proforma revenue requirements as per Respondent's Exhibit 8 are in the sum of

$102,000.83; the operating revenues for 1966 amounted to $95,511.00; there is a need for increased revenues in the sum of $6,572 for the combined water and sewer of Respondent;

(11) the rates proposed by Respondent in this proceeding for water and sewer service are unjust and unreasonable and would yield an excessive rate of return based on the fair value of Respondent's property used and useful in rendering water and sewer service and should be modified only to provide additional operating revenue in the sum of $6,572.

It Is Therefore Ordered that the schedules of rates, rules and regulations designated as Ill. C.C. No. 2, 3rd Revised Sheet No. 1, and Ill. C.C. No. 1, 1st Revised Sheet No. 1, filed with this Commission by Du Page Utility Company on February 20, 1967, be, and the same is hereby, cancelled and annulled.

It Is Further Ordered that Du Page Utility Company is hereby authorized and directed to file revised schedules of rates to provide additional operating revenue in a sum not to exceed $6,572.

It Is Further Ordered that all objections and motions made in this proceeding which remain undisposed of shall be considered disposed of and resolved consistent with the ultimate conclusions herein contained.

By Order of the Commission this 17th day of January, 1968.

/s/ James W. Karber,
Chairman

(SEAL)
RLT/jh

STATE OF ILLINOIS
ILLINOIS COMMERCE COMMISSION

DU PAGE UTILITY COMPANY In the matter of the proposed revisions in rates for sewer service, stated in 3rd Revised Sheet No. 1, Ill. C.C. No. 2	53105
DU PAGE UTILITY COMPANY In the matter of the proposed revisions in rates for water service, stated in 1st Revised Sheet No. 1, Ill. C.C. No. 1	53106

APPLICATION FOR REHEARING

To the Illinois Commerce Commission:

Comes now Du Page Utility Company, Respondent in the above entitled proceeding (hereinafter sometimes referred to as "Respondent" or "Company") and applies to this Honorable Commission for rehearing and reconsideration in respect to the matters determined by the order of this Commission entered in this proceeding on January 17, 1968 (the "order"), and, in support of such application, sets forth and relies upon the grounds and reasons hereinafter in this application contained.

1. The order cancelling and annulling the rates filed by Respondent on February 20, 1967 (Ill. C.C. No. 1, 1st Revised Sheet No. 1, and Ill. C.C. No. 2, 3rd Revised Sheet No. 1) and directing Respondent to file and place into effect rates to provide additional operating revenues of only $6,572 is erroneous, contrary to law, confiscatory, discriminatory, arbitrary and contrary to and without support in the evidence introduced in this proceeding.

2. The purported recitals of fact, the findings of fact and the conclusions thereon contained in said order are wholly insufficient to sustain the said order of the Commission and are erroneous, contrary to law and contrary to and without support in the evidence introduced in this proceeding.

3. Said order is erroneous and contrary to law in that it fails to make findings or recitals of fact and conclusions thereon with respect to material, substantial and uncontroverted evidence submitted by the Respondent and received by the Commission.

4. Said order is erroneous and contrary to law in that it contains purported recitals of fact, findings of fact and conclusions thereon which are contrary to the manifest weight of and without any support whatsoever in the evidence received by the Commission.

5. Said order is erroneous and contrary to law in that the purported recitals of fact, findings of fact and conclusions thereon made by the Commission express mere conclusions not based upon any facts found by it and are not a sufficient basis for said order of the Commission.

6. Said order is erroneous and contrary to law in that the Commission in Finding (9) found the Company's fair value rate base is no greater than $13,235.36, whereas in Finding (7) it found that the working capital requirements of the Company which are by law the part of fair value rate base to be $15,625.50.

7. Said order is erroneous and contrary to law in that in purporting to determine a fair value rate base no allowance whatsoever was made for any value for the physical plant and property of Respondent, which the Com-

mission found to have a total net original cost of $787,701.17 and a reproduction cost new less depreciation of $887,304.69.

8. Said order is erroneous, contrary to law and contrary to the evidence received by the Commission in the proceeding in that in purporting to determine the fair present value of Respondent's utility plant for rate-base purposes, it failed to give any consideration or weight to the reproduction cost new or reproduction cost less depreciation of Respondent's utility plant, as required by law of Illinois and the Constitutions of the State of Illinois and the United States of America.

9. Said order is erroneous, contrary to law and contrary to the evidence received by the Commission in the proceeding in that it failed to make any finding of fact (or recital of fact adopted as a finding of fact) as to the fair present value of Respondent's utility plant, after a full and proper consideration of all the factors of rate-base valuation, including original cost of construction, reproduction cost new, working capital requirements, operating expenses, depreciation, reserves necessary in good business judgment and operations, a reasonable return to the investor on the basis of the present fair value of the property, and a reasonable return sufficient to assure the financial integrity of the Company, maintain its credit and to attract new capital, as required by the law of Illinois and the Constitutions of the State of Illinois and the United States of America.

10. Said order is erroneous, contrary to law and contrary to the evidence received by the Commission in the proceeding in that in determining the present fair value of Respondent's utility plant for rate-making purposes it

failed to give any weight to the original cost of construction of such utility plant.

11. Said order is erroneous and contrary to law in that it failed to fix and determine any rate of return on the purported fair value rate base as contained in Finding (9).

12. Said order is erroneous and contrary to law in Finding (10) that "Respondent's proforma revenue requirements as per Respondent's Exhibit 8 are in the sum of $102,000.83" in that such finding is entirely contrary to and without support in the evidence adduced by the Commission.

13. Said order is erroneous, contrary to law and contrary to and without support in the evidence introduced in the proceeding in that it contains the following findings of fact:

• • •

17. Said order is erroneous, contrary to law, and contrary to the evidence received by the Commission in the proceeding in that it failed to make any finding of fact (or recital of fact adopted as a finding of fact) as to the rate of return upon the present fair value of the Company's utility plant which would result from application of the rates directed by the Commission order.

• • •

19. Said order will prevent the Company from charging and receiving just compensation for the use of its property and constitutes the taking of the property of the Company without due process of law and such order is, therefore, confiscatory in nature and effect, in consequence of which it constitutes a violation of Sections 2 and 13 of Article II of the Constitution of the State of Illinois

and, also, constitutes a violation of Article XIV, Section 1 of the Articles in addition to and amendment of the Constitution of the United States of America.

20. The proceedings and action on the part of the Commission in failing to fix, determine and prescribe the rates for water service in Ill. C.C. No. 1, First Revised Sheet No. 1, and the rates for sewer service proposed by Respondent in Ill. C.C. No. 2, Third Revised Sheet No. 1, filed herein on February 20, 1967, will prevent Respondent from charging and receiving just compensation for the use of its property and constitute a taking of the property without due process of law and are, therefore, confiscatory in nature and effect, in consequence of which they constitute a violation of Sections 2 and 13 of Article II of the Constitution of the State of Illinois and, also, constitute a violation of Article XIV of Section 1 of the Articles in addition to and amendment of the Constitution of the United States of America.

21. The proceedings and action on the part of the Commission in failing to fix just and reasonable rates upon the fair value of Respondent's property used and useful in rendering service to the public in its order will prevent Respondent from charging and receiving just compensation for the use of its property and constitutes a taking of the property of the Company without due process of law and are, therefore, confiscatory in nature and effect, in consequence of which they constitute a violation of Sections 2 and 13 of Article II of the Constitution of the State of Illinois and, also, constitute a violation of Article XIV of Section 1 of the Articles in addition to and amendment of the Constitution of the United States of America.

Wherefore, the Company prays that the Commission grant it a further rehearing in the above entitled cause to the end that the errors above set forth may be corrected and that the schedules of rates filed by the Company on February 20, 1967 be made effective for all bills rendered for water service and for sewer service, thus affording the Company a sufficient amount available for return after proper expenses to more nearly provide that reasonable return upon the present fair value of its plant and property used and useful in rendering service to the public as guaranteed by the Constitutions of the State of Illinois and of the United States of America and as prescribed by the Illinois Public Utilities Act.

Respectfully submitted,

DU PAGE UTILITY COMPANY

STATE OF ILLINOIS
ILLINOIS COMMERCE COMMISSION

Du Page Utility Company In the matter of the proposed revisions in rates for sewer service, stated in 3rd Revised Sheet No. 1, Ill. C.C. No. 2	53105
Du Page Utility Company In the matter of the proposed revisions in rates for water service, stated in 1st Revised Sheet No. 1, Ill. C.C. No. 1	53106

ORDER ON REHEARING

By the Commission:

On February 20, 1967, Du Page Utility Company (hereinafter sometimes referred to as "Respondent") filed with this Commission its rate schedule for sewer service, designated Ill. C. C. No. 2, 3rd Revised Sheet No. 1, and its rate schedule for water service, designated Ill. C. C. No. 1, 1st Revised Sheet No. 1, proposing general increases in sewer and water rates to be effective March 22, 1967.

* * *

The Commission entered its order on January 17, 1968, denying the rate increase sought by the Respondent. The Respondent and the Intervenors both filed their applications for Rehearing which were granted by the Commission on February 27, 1968. Pursuant to notice to all parties entitled to same a rehearing was held on March 11, 1968, at Chicago, Illinois, before a duly authorized Examiner of the Commission. At said rehearing, the Respondent presented further evidence concerning the installation of fluoridation equipment and additional operating expense in connection therewith as required by recent legislative action and in addition both the Respondent and Intervenors stood on their previous record in these proceedings. At the conclusion of said rehearing the matter was again marked "Heard and Taken."

Du Page Utility Company provides water and sewage disposal service to approximately 840 customers consisting mostly of residential customers in Oak View Subdivision in the Village of Lisle,

Illinois, and the Meadows Subdivision immediately south of the Village in Du Page County, Illinois. A few commercial customers are included in a shopping center area and a recreation area known as Four Lakes, also near the Village of Lisle, in Du Page County.

Respondent obtains its water supply from two wells connected to a common distribution system. Initially it owned and operated a sewage treatment plant which was sold to Du Page County in 1961. Respondent now pays Du Page County a specific rate to handle its sewage treatment, which rate is subject to an increase commencing May 1, 1968.

Sewage disposal service is presently rendered by Respondent to single-family residences at a flat rate of $2.50 per month or $7.50 per quarter. The proposed new rate is $4.50 per month or $9.00 per two-month period. Service to multi-family, commercial and institutional users is presently rendered at a rate of $ .50 per 1,000 gallons of water used per month as per meter reading or the flat rate presently charged single-family residences, whichever is greater. Under the proposed rate the charge is $ .45 per 100 cubic feet of water used per month as per meter reading or the new flat rate proposed to be charged single-family residences, whichever is greater. The proposed schedule continues the 10% delayed payment charge and also provides that any connection charge imposed by the County of Du Page, which furnishes sewage treatment service to the Company, shall be paid by the customer to said County prior to commencement of service.

General metered water service is presently rendered in Lisle and vicinity by the Company under the following rates:

First 3,000 Gals. or less per month or 9,000 Gals. or less per quarter $.75 per 1,000 Gals.
Next 5,000 Gals. per month or 15,000 Gals. per quarter $.60 per 1,000 Gals.
Over 8,000 Gals. per month or 240,000 Gals. per quarter $.45 per 1,000 Gals.

The proposed rates for metered water service are as follows:

First 1,000 Cu. ft. per 2 month period $.84 per 100 Cu. ft.
Next 1,000 Cu. ft. per 2 month period $.70 per 100 Cu. ft.
Next 3,000 Cu. ft. per 2 month period $.56 per 100 Cu. ft.
Over 5,000 Cu. ft. per 2 month period $.40 per 100 Cu. ft.

The present minimum water bill is $2.25 per month or $6.75 per quarter. The proposed minimum bill per 2 month period is $8.40, for which up to 1,000 cubic feet of water will be allowed without additional charge. Presently, most customers are billed quarterly. The Company proposes to bill most customers per 2 month period, but reserves the right to bill monthly, in which case the rate blocks and minimum bill shall be one-half of those for the 2 month period above stated. The proposed schedule continues the 10% delayed payment charge.

The Illinois Supreme Court has held that just and reasonable rates are predicated upon the present fair value of the utility property, and must be sufficient to provide for operating expenses, depreciation, reserves that are necessary in good business judgment and operations, and a reasonable return

to the utility on the basis of the fair value of the utility property. In order to determine such fair value the Commission is required to take into account current economic conditions, price levels and reproduction cost, as well as the original cost of construction, the amount expended in permanent improvements and the probable earning capacity of the property under the particular rates prescribed. *Illinois Bell Telephone Company* v. *Illinois Commerce Commission*, 414 Ill. 275.

Original Cost

The Respondent presented oral testimony and documentary evidence of original cost of utility plant. It presented the testimony of an experienced utility accountant and offered in evidence Respondent's Exhibit 8 showing the total original cost of the Company's water and sewer utility plant in service as of December 31, 1966, to be $875,418.55. Said amount is comprised of water utility plant in service of $528,059.65, and sewer utility plant in service of $347,358.90. To the water utility plant, upon rehearing was added the sum of $909.35 for fluoridation equipment required by recent legislative action, resulting in an adjusted utility plant in service of $876,327.90. The Company's witness testified that the original cost of the utility plant was fixed by the order of this Commission entered November 27, 1963, in Ill. C. C. Docket No. 49962 (Respondent's Exhibit 6) and adjusted by subsequent acquisitions and retirements of plant as reflected by the books of the Company and upon information supplied to him by management.

Respondent's Exhibit 8 further shows that the total accumulated depreciation for utility plant was $87,717.38, and that, after deducting such reserve

from the original cost, the total net original cost of utility plant in service as of December 31, 1966, was $787,701.17. Said Exhibit further shows that the depreciation on water plant is $52,659.18 and that net water plant in service is $475,400.47; that depreciation on sewer plant is $35,058.20 and that net sewer plant in service is $312,300.70.

Respondent's Exhibit 8 (Schedule I) presents a balance sheet as of December 31, 1966. It shows an item of Customers Advances for Construction. The Company's expert witness testified that this item represents unrefunded balance of certain advances made for construction of facilities to serve the Four Lakes area and that under the contract, further refunds may accrue so that the balance may be refunded entirely.

The Company's expert witness also testified that the item of Extraordinary Property Losses represents the difference between the original cost and the sales price of the sewage treatment plant sold to the County of Du Page. Said item is in litigation between the Company and the Commission and is being provided for in a separate reserve out of income. The Company, however, reserves the right to charge it as an operating expense in the event that the Commission's order is reversed.

The Company's expert accounting witness testified that a balance sheet item of capital in excess of par value of shares in the amount of $892,591.42, shown on Respondent's Exhibit 8 (Schedule I), was properly recorded in the capital account and was not a contribution in aid of construction. He stated that said item was capital surplus comprising cash donations to capital of the Company by interests

affiliated with the common shareholders of the Company, and included a land development company. Officers of the Company testified that no part of the purchase price received by the affiliates from the sale of lots or houses was used for the payment of the cost of installation of water and sewer lines to said lots, that said cost was not charged to the purchasers, that there was no allocation of the cost of utility plant to the purchase price of a house or lot, and that water and sewer facilities had been already installed prior to the sale of the houses or lots.

Upon cross examination of the officers-directors of the Respondent it was developed that the three shareholders each initially invested $5,000 cash for 50 shares respectively, of the capital stock of Du Page Utility Company, which represents all the issued and outstanding stock of the utility. None of the shareholders personally invested any funds in the utility company other than the initial $5,000 paid for stock. The same three shareholders were also initially partners and subsequently equal shareholders in the Oak View Improvement Company which was a corporation engaged in the development of the real estate serviced and to be serviced by Du Page Utility Company. Oak View Improvement Company sold both improved and unimproved lots in the Meadows and Oak View subdivisions, and prospective purchasers were informed that all improvements, including sewer and water, were included in the price of the lots. A form of contract between Oak View Improvement Company and a purchaser was admitted into evidence as Intervenor's Exhibit No. 5, which by its terms provided that improvements, in-

cluding sewer and water, were in and fully paid for and no assessments would be levied therefor. Funds from the sale of lots in the subdivision were deposited to a bank account maintained by Oak View Improvement Company and some of these funds were subsequently transferred to the Respondent and used by the Respondent to build its water and sewerage plant. These funds received from Oak View Improvement Company and its successor, Kepler & Clark, Ltd. were carried on Respondent's books and records on a ledger sheet entitled "Contributions in Aid of Construction", a copy of which ledger sheet was received into evidence as Intervenor's Exhibit No. 3, which reflected a closing balance of $793,195.25 as of September, 1966. The Respondent's accountant testified that he changed the designation of that account on December 31, 1966, from "Contributions in Aid of Construction" to "Capital in Excess of Par Value of Shares." It was also established on cross examination by the Accounting Staff of the Commission that in Ill. C. C. Docket No. 50409 involving the Respondent, the then auditor for the Company testified that funds received from purchasers for the sale of the lots by Oak View Improvement Company were treated as expense by that company and that the funds used to develop the sewer and water systems were carried as an element of the cost of the land by the affiliated Oak View Improvement Company and that the contributions made by Oak View Improvement Company to Du Page Utility Company were considered as a development cost and prorated over the lots to be sold and expensed to those units as they were sold. Respondent's president admitted that the transactions had been handled in that manner.

Respondent's Federal Income Tax return for the year 1966 was also admitted into evidence as Intervenor's Exhibit No. 1 and indicated that about 91.24% of the taxpayer's Respondent's assets were reported to the Internal Revenue Service as having a zero tax basis in accordance with Section 362(C) of the Internal Revenue Code (Staff Exhibit 1) which provides in effect that property constructed with such moneys donated to a corporation by persons other than the shareholder has a zero basis for income tax purposes and may not be depreciated.

A certified public accountant testified on behalf of the Intervenors that he was familiar with The Uniform System of Accounts for Water Utilities as prescribed by the Illinois Commerce Commission and was also familiar with the definition of "paid in surplus" under the Business Corporation Act of Illinois and that in his opinion "Contributions in Aid of Construction" were neither stated capital nor paid in surplus as defined by the Illinois Corporation Act, whereas donations made by shareholders or proprietary capital in excess of par value of shares should be considered either Stated Capital or Paid in Surplus under that Act. Certified copies of the Annual Reports filed by the Respondent with the Secretary of State of the State of Illinois were admitted into evidence as Intervenor's Exhibit No. 2, and reflected that during the years 1962 through 1967 inclusive, the Respondent reported no paid in surplus and showed as its sole capital $15,000 of Stated Capital. The annual reports were consistent with the treatment of funds received from Oak View Development Company, or other affiliated companies as "Contributions in Aid of Construction" by the Respondent as

was the fact that almost all assets of the corporation had a zero basis for Federal Income Tax purposes.

A witness for the Accounting Staff of the Commission proposed that $793,195.25 be reclassified from capital surplus to contributions in aid of construction and be deducted from the original cost of the Company for rate base determination, resulting in a zero or negative original cost component of rate base.

The Commission concurs with this reclassification. Under the real estate sales contract sewer and water was included in the purchase price, and based on the treatment accorded such sums by the Respondent in its books and records, Federal Income Tax returns, Annual Reports to the State of Illinois under the Illinois Business Corporation Act and the treatment of said funds by the Oak View Development Company, said funds are rightfully contributions in aid of construction and not capital surplus. Such classification was affirmed by the Illinois Supreme Court in *Killarney Water Co., et al.* v. *Illinois Commerce Commission,* 37 Ill. 2d 345. In that case the Court also stated that "The significance of the way the parties to a transaction treat it for tax purposes, as indicating their intention is pointed out in *Hammer* v. *Sanders,* 8 Ill. 2d 414 at 421."

The attempt by a utility to restore to the rate base the cost of water or sewer lines written off for tax purposes as land development costs was determined in a recent Florida case, *Westwood Lake, Inc.* v. *Metropolitan Dade County Water & Sewer Board,* 71 PUR 3rd 260 (Fla. D. Ct. of Appeal, 3rd District). In that case the court sustained the exclusion of moneys contributed by the purchasers of

lots for the water mains from the rate base based on the treatment accorded these funds by the development companies in excluding the funds on their tax returns and on their unqualified certified audits and reports to the Board.

Reproduction Cost New

Respondent's Exhibit 8 (Schedule III) shows the reproduction cost new and reproduction cost new less depreciation of the Company's property used and useful in providing water service as of December 31, 1966. The Company's expert witness testified that reproduction cost new was calculated by trending the original cost of the Company's utility plant in service by use of the Handy-Whitman Indices of Plant and Construction Costs for the North Central Area of the United States. These indices were applied to all plant except land and organization costs, which two classifications were not trended. By this method an estimated total reproduction cost new, as of December 31, 1966, of $986,322.74 was developed. Said figure consists of $600,545.79 for water plant and $385,776.95 for sewer plant. This method of determining reproduction cost new has been employed in many other cases and accepted by this Commission. To this figure of reproduction cost new the witness then applied the same percentage of depreciation as appeared on the books with relation to accrued depreciation to utility plant in service and, as a result, computed the total reproduction cost new less depreciation to be $887,304.69. The net reproduction cost new of the water plant in service is $540,491.21, and the net reproduction cost new of the sewer plant in service is $346,813.48. To the foregoing may be added the further sum

of $909.35 for the fluoridation equipment resulting in an adjusted reproduction cost new less depreciation of $888,214.04.

Cash Working Capital

Respondent's Exhibit 8 (Schedule VIII, Revised) presents an estimate of a proper allowance for cash working capital in the amount of $18,880.00. The Company's expert witness testified that the working capital requirement is based upon an average 2½ months operating expenses, on a pro forma basis, not including depreciation, operating taxes, Federal Income Tax, and rate case expense. The period chosen is based upon the proposed bimonthly billing period plus 15 days collection. No accrued tax items or similar accruals were deducted because, as the witness testified, the Company has no material accruals of such nature.

The working capital requirement of Respondent as adjusted by the disallowance of part of officers' salaries (referred to elsewhere in this Order) and by the additional expense of operation of the fluoridation equipment may be computed as follows:

Annual Requirements (per Schedule VIII Revised, Resp. Ex. 8)	$91,884.00
Additional (per Resp. Ex. 1 on Rehearing)	3,418.00
	$95,302.00
Less: Officers' salaries disallowed	15,840.00
Adjusted Annual Requirement	$79,462.00
Monthly Requirement	$ 6,622.00
2-1/2 Months Requirement	$16,555.00

Fair Value

The Commission has reviewed the elements of a fair value rate base of the Company as submitted in evidence. It is the duty and prerogative of the Commission to determine a fair value rate base after giving full and proper consideration to all the evidence as to (1) original cost, (2) reproduction cost, (3) a proper allowance for depreciation, (4) cash working capital requirements and (5) all other elements of value which have been shown by the evidence in the case relating to value. On the basis of the evidence received herein, the Commission finds that the fair value of the Company's property used and useful in rendering water service and sewerage disposal service to the public for rate-making purposes is about $16,555.00.

Rate of Depreciation

For the purpose of computing its operating expenses and the utility operating income which would result from the rate schedule proposed by the Company in this case, the Company claims an allowance for depreciation at the approximate composite rate of 1.6% of the original cost of depreciable plant. The Commission is of the opinion that for the purpose of the instant case in determining rates for water and sewer service such depreciation rate is fair and reasonable.

Regulatory Commission Expense

The total costs of the present proceeding were reasonably estimated by the Company to be $15,000, which sum the Company proposed to amortize over a 5-year period at the rate of $3,000 annually. Legitimate regulatory Commission expense incurred by a utility is part of the cost of doing business and, hence, recoverable. The Commission is of the opinion

and here prescribes that the cost of this proceeding be entered on the books of the Company as a deferred debit, which debit shall be credited with such amount annually as shall be required to amortize said amount in equal installments over a 5-year period.

Operating Revenues and Deductions

The total gross operating revenues of the Company for the 12 months ended December 31, 1966 (used as the test year for purposes of this case) were $95,511.04, and total operating expense deductions for the same period, including provision for Federal Income Taxes, were $106,243.69, resulting in total net operating loss of $10,732.65. With respect to water service operations, gross operating revenues for the test year were $66,228.82, operating expense deductions were $66,654.10, resulting in a net operating loss of $425.28. With respect to sewerage disposal service operations, gross operating revenues for the test year were $29,282.22, operating expense deductions were $39,589.59, resulting in a net operating loss of $10,307.37. Respondent's Exhibit 8 (Schedule IV) shows that the Company has experienced a net operating loss every year since 1962 and had a retained earnings deficit as of December 31, 1966, of $81,549.38.

Respondent's Exhibit 8 (Schedule VII) adjusts the operating revenue and operating expense figures for the test year to reflect pro forma changes under its proposed rates. The Company's expert witness stated that Schedule V thereof is a bill analysis of actual billings and revenues of the Company under present rates, which is summarized in Respondent's Exhibit 9. Schedule VI of Respondent's Exhibit 8 is a projection of revenues under the proposed rates, based upon said bill analysis. Schedule VII includes

this pro forma adjustment to operating revenue as well as the pro forma adjustment to operating expense detailed in Respondent's Exhibit 10.

A witness for the Accounting Staff of the Commission proposed that the pro forma operating income of the Company be adjusted by disallowing for rate-making purposes one-half of the annual Officers' salaries. Such adjustment would increase pro forma operating income by $15,840 to $44,997. He stated that he reviewed the salaries paid to Officers of the Company in light of salaries paid to officers of other companies under the Commission's jurisdiction.

The Respondent's three officers, who are also the sole stockholders of the Company, each testified as to the nature and extent of work they respectfully performed for the Respondent. Each, however, was an officer and engaged actively in the operation and management of other companies. The Commission finds that the Officers' salaries are unreasonably disproportionate to the nature and extent of work performed by them, and compared to salaries paid to full-time management officials of water utilities of similar size under its jurisdiction.

Schedule VII Revised of Respondent's Exhibit 8 shows that if the proposed rates had been in effect during the test year, the pro forma adjustments result in net operating income of $26,556.00 under the proposed rates after deducting operating expenses of $129,001.00 from operating revenues of $155,557.00. The total operating expense is increased to about $130,788 after being adjusted by the fluoridation expense of about $3,436.00, less the related federal income tax on said amount of about $1,649.00. This

decreases the total pro forma net operating income under the proposed rates to about $24,769.00. With respect to water service operations as adjusted by the fluoridation expense under the proposed rates, there would result pro forma operating revenues of about $102,073.00, operating expenses of about $78,732, and net operating income of about $23,341.00 With respect to sewerage disposal service under the proposed rates, there would result pro forma gross operating revenues of about $53,484.00, operating expenses of $52,056.00, and net operating income of $1,428.00. Such estimates include computation of revenues from all possible customers of the Company for the full test year based upon the number of services attached at the end of the test year.

Rate of Return

A witness for the Company testified that he made a study of earnings experienced for the years ending December 31, 1964, and December 31, 1965, by representative water companies in the Illinois area or neighboring states, whose earnings were reported in Moody's Public Utility Manual for the years 1965 and 1966. He computed operating income after Federal income taxes but before debt service charges; he computed net plant as utility plant net of deduction for accumulated depreciation. He then computed the earnings on net plant for each company, being the ratio of operating income and net plant so stated. He also determined the weighted average earnings on net plant, by computing the ratio of total operating income and total net plant for the companies studied. This investigation shows that 6.39% in 1964 and 6.13% in 1965 were the average earnings on net plant for the representative water companies.

The Commission having considered all of the evidence, both oral and documentary, introduced at the hearings in this matter and being fully advised in the premises, is of the opinion and finds that:

(1) Du Page Utility Company is engaged in furnishing water and sewage disposal service in certain areas in the Village of Lisle, Du Page County, Illinois, and vicinity, and is a public utility within the meaning of an Act entitled "An Act concerning public utilities," as amended; the Commission has jurisdiction of the parties and of the subject matter herein;

• • •

(5) for the purpose of this rate case, the original cost of Respondent's water plant and property used and useful in rendering service to the public, as of December 31, 1966, was $528,059.65, and the provision for depreciation was $52,659.18, resulting in a net original cost depreciated as of December 31, 1966, of $475,400.47, and adjusted by the inclusion of fluoridation equipment totals $476,309.82; the original cost of Respondent's sewage disposal plant used and useful in rendering service to the public as of December 31, 1966, was $347,358.90, and the accumulated provision and depreciation on said net plant was $35,058.20, resulting in a net original cost depreciated for the sewage disposal plant, as of December 31, 1966, of $312,300.70; the total net original cost for both the water and sewage disposal plant and property depreciated as adjusted for the purpose of these proceedings was $788,610.52.

(6) the reproduction cost new of the used and useful property of Du Page Utility Company, as

of December 31, 1966, and adjusted by the inclusion of the fluoridation equipment was $987,232.09, which less an allowance for depreciation of $99,018.05, would result in reproduction cost new less depreciation, as adjusted of $888,214.04; that the reproduction cost new, as of December 31, 1966, and adjusted by the inclusion of fluoridation equipment, of Du Page Utility Company's plant and property used and useful in providing water service was $601,455.14, the reserve for depreciation was $60,054.58, and net reproduction cost new was $541,400.56; that the reproduction cost new, as of December 31, 1966, of Du Page Utility Company's plant and property used and useful in providing sewerage disposal service was $385,776.95, the reserve for depreciation was $38,963.47, and net reproduction cost new was $346,813.48;

(7) the salaries of the officers in the sum of $31,680 was excessive and that a more reasonable amount for officers' salaries for the service performed would be 1/2 that amount or the sum of $15,840; that with the adjustment of officers' salaries the working capital requirements of the Respondent as adjusted upon rehearing is $16,555.00 for seventy-five (75) days;

(8) the sum of $793,195.25 representing cash contributions from interests affiliated with the shareholders of Respondent constitutes "contributions in aid of construction" and not capital surplus, and that said sum together with additional contributions in aid of construction in the aggregate amount of $798,702.25 should be deducted from the cost of utility plant in service in computing its fair value for rate making purposes;

(9) for the purpose of this proceeding, the Company's fair value rate base was no greater than about $16,555;

(10) in determining a fair rate of return which should be applied to the fair value rate base herein, the Commission has considered all the evidence in the record, current economic conditions, the rate of return of other enterprises having a corresponding risk, equity capital and the principles of law governing the determination of just and reasonable rates for utilities, as stated by the Supreme Court of the State of Illinois, and has concluded therefrom that a rate of return of about 6.5% is fair and reasonable;

(11) Respondent's pro forma revenue requirements as per its Revised Exhibit 8 and adjusted by the addition of the fluoridation expense and certain tax adjustments, less that portion of the officers' salaries disallowed and Federal Income Tax therefor as adjusted, total about $109,240; the 1966 revenues are about $95,511, reflecting a need for an increase of about $13,729 to provide operating revenues sufficient to cover operating expenses and return on fair value rate base, all as set forth in Appendix B attached hereto and made a part of this order

(12) the presently effective rates for water and sewer service furnished by Du Page Utility Company are unjust and unreasonable since said rates do not provide sufficient operating revenues to pay for reasonable operating expenses and a fair and reasonable return on the fair value of the Company's used and useful property in furnishing water and sewer service to the public;

(13) the rates proposed by the Du Page Utility Company in this proceeding are unjust and unreasonable, and would yield an excessive return, and should be modified as hereinafter set forth;

(14) the rates set forth in Appendix C attached hereto and made a part of this Order are just and reasonable, and should be placed in effect as the legal rates for water and sewer service furnished by Du Page Utility Company; said rates are also designed to bring the rates for sewer service in balance with those for water service so far as the general financial condition of the Company is concerned;

(15) the rates set forth in Appendix C should become effective for current unbilled service on five (5) days' notice.

It Is Therefore Ordered that the schedules of rates set forth in Appendix C hereto attached and made a part hereof be, are hereby approved, and Du Page Utility Company is authorized to place same in effect as its schedules of rates for water and sewer service.

• • •

By order of the Commission this 16th day of April, 1968.

Commissioner Robert E. Dolph dissents by formal written opinion.

Commissioner Robert E. Dolph, dissenting:

The application of the theories of the Uniform System of Accounts to rate making procedures for water and sewer utilities, has always been, in my opinion, anathema to equity and good conscience.

The case at bar, is very much in point and demonstrates the futility of our historic treatment of "contributions in aid of construction". A similar fallacy arises when we treat a developers "expensing" plant construction in the same way. It seems to me that we are looking at the wrong law for enforcement.

The fact is, that a plant of value is being used daily by the rate-payers, and granted the event of

effective, good service, the rate-payers ought to pay a rate commensurate with the value of the plant they use.

We say in this case that it would cost almost a million dollars to replace this plant and that it cost more than $800,000 to build in the first place and yet, by what I believe to be antiquated and inapplicable accounting procedures this Commission has arrived at the conclusion that $16,555 is a fair value rate base. What do we use for a formula when that last figure becomes zero?

I believe the unfairness comes when we try to mold ourselves too much to a format which was designed for other utilities. These rules were designed for the use of gas and electric and other utilities in their mergers. Those utilities are a completely different breed of cat.

Of greatest importance is the value of "availibility" of a central sewerage treatment facility and the value of a central water distribution system. The knowledge that these will exist is certainly distinct from any form of ownership in their existence except for a specific contractual relationship spelled out between the developer and the purchaser. This was done in our Lake Holiday Case.

With the speculation inherent in orders of this kind, the rate base might well be a minus figure or after an Internal Revenue investigation an "expensed" item may be completely redlined and stricken by that agency. Could we then go to the purchaser for some additional contribution?

There is in my opinion more merit in the conclusion that a homeowner buys a package when he buys his home. The package includes many

things—including the availability of central sewerage treatment so that an individual septic tank is unnecessary, and the availability of central water distribution so that a private well is unnecessary. All of which can be clearly set out in the terms of a contract (Lake Holiday Case).

The social significance of efficiently operated water and sewer companies in the spectre of pollution-laden streams in Illinois cannot be exaggerated. This requires a sound financial structure. That structure requires equitable rates.

The greatest problem for these rate-payers will come when service dwindles to the point where municipal ownership will be desired. Then condemnation will become involved. What will any Sanitary Engineer testify to as the "Current" value of this plant. That is the price the municipality will pay.

In my opinion, we should reject the Uniform System of Accounts in these cases and adopt a formula that is realistic, keeping in mind that the law of Illinois requires us to arrive at a "fair value" rate base and that other formulas are inapplicable here.

APPENDIX A

COMPUTATION OF FAIR VALUE RATE BASE

	Original Cost	Reconstruction Cost New	Fair Value
Utility Plant in Service			
Water	$528,059.65	$600,545.79	
Fluoridation Equipment	909.35	909.35	
Sewer	347,358.90	385,776.95	
Total Plant	$876,327.90	$987,232.09	
Less: Accrued Depreciation			
Water	$ 52,659.18	$ 60,054.58	
Sewer	35,058.20	38,963.47	
Total Reserve	$ 87,717.38	$ 99,018.05	
Net Utility Plant in Service	$788,610.52	$888,214.04	
Weighting Factor	75%	25%	
Weighted Cost	$591,457.89	$222,053.51	$813,511.40
Deduct:			
Customer's Advances for Construction		$ 15,669.64	
Contributions in Aid of Construction		798,702.25	
Unamortized Investment Credit		620.30	814,992.19
Fair Value of Utility Plant for Rate Base			- 0 -
Add: Working Capital Requirements [1]			$ 16,555.00
Fair Value Rate Base			$ 16,555.00

[1] Computation of Working Capital Requirements

Annual Requirements (per Resp. Ex. 8, Schedule VIII Revised)	$ 91,884.00
Additional (per Resp. Ex.1-Rehearing)	3,418.00
Total	$ 95,302.00
Less: Officers' Salaries Disallowed	15,840.00
Adjusted Annual Requirement	$ 79,462.00
Monthly Requirement	6,622.00
2½ Month Requirement	$ 16,555.00

APPENDIX B

DU PAGE UTILITY COMPANY

REVENUE REQUIREMENTS

Rate of Return			
Fair Value Rate Base		$16,555	
Rate of Return		.065	
			$ 1,076
Operating Expenses			
Per Resp. Ex. 8, Sch. VII Rev.		$129,001	
Add: Fluoridation Expenses		3,436	
		$132,437	
Less: Federal Income Tax	$12,167		
Officers' Salaries Disallowed	15,840	28,007	
		$104,430	
Add: Federal Income Tax			
Net operating Income	1,076		
Excess of Book Depreciation over tax Depreciation	12,165		
Federal Income Tax	3,734		
Taxable Income	$16,975		
X 22%		3,734	$108,164
Revenue Requirements			$109,240
1966 Revenues			95,511
Increase Required			$ 13,729

APPENDIX C

DU PAGE UTILITY COMPANY
WATER SERVICE

METERED WATER SERVICE

Available to customers receiving water service by meters.

RATES

First 800 cubic feet per 2-month period $.58 per 100 cu. ft.

Next 1332 cubic feet per 2-month period $.47 per 100 cu. ft.

All over 2132 cubic feet per 2-month period $.28 per 100 cu. ft.

MINIMUM BILL

The minimum charge per 2-month period shall be $4.64 for which up to 800 cubic feet of water shall be allowed without additional charge.

The Company reserves the right to bill either monthly or per 2-month period but in case of monthly billing, the rate blocks and minimum bill shall be one-half of those above stated.

DELAYED PAYMENT CHARGE

An additional charge amounting to 10% of the net bill will be added to all bills for water service not paid within 10 days of the date of the bill.

SEWERAGE DISPOSAL SERVICE

SEWERAGE DISPOSAL SERVICE
RATE APPLICABLE TO
SINGLE FAMILY RESIDENCES

Sewerage disposal service available only to premises wherein the property or utility easement line abuts the installed sanitary sewer mains of the Company.

Net Flat Rate: $3.50 per month or $7.00 per two-month period.

The Company reserves the right to bill either monthly or per two-month period.

RATE APPLICABLE TO MULTI FAMILY, COMMERCIAL AND INSTITUTIONAL USERS

Available only where water service is furnished by meter.

The net rate or charge to the customer shall be $0.42 per 100 cubic feet of water used per month as per meter reading or the net flat rate for single-family residence customers, whichever is greater.

DELAYED PAYMENT CHARGE

An additional charge amounting to 10% of the net bill will be added to all bills for sewerage disposal service not paid within 10 days of the date of the bill.

CONNECTION CHARGES

Any connection charge imposed by the County of Du Page (which furnishes sewage treatment service to the Company) shall be paid by the customer to said County prior to commencement of service.

STATE OF ILLINOIS
ILLINOIS COMMERCE COMMISSION

DU PAGE UTILITY COMPANY In the matter of the proposed revisions in rates for sewer service, stated in 3rd Revised Sheet No. 1, Ill. C.C. No. 2	53105
DU PAGE UTILITY COMPANY In the matter of the proposed revisions in rates for water service, stated in 1st Revised Sheet No. 1, Ill. C.C. No. 1	53106

APPLICATION FOR REHEARING

To the Illinois Commerce Commission:

Comes now Du Page Utility Company, Respondent in the above entitled proceeding (hereinafter sometimes referred to as "Respondent" or "Company")

and applies to this Honorable Commission for rehearing and reconsideration in respect to the matters determined by the Order on Rehearing of this Commission entered in this proceeding on April 16, 1968 (the "order"), and, in support of such application, sets forth and relies upon the grounds and reasons hereinafter in this application contained.

1. The order cancelling and annulling the rates filed by Respondent on February 20, 1967 (Ill. C.C. No. 1, 1st Revised Sheet No. 1, and Ill. C.C. No. 2, 3rd Revised Sheet No. 1) and directing Respondent to file and place into effect rates set forth in Appendix C thereof to provide additional operating revenues of only $13,729 is erroneous, contrary to law, confiscatory, discriminatory, arbitrary and contrary to and without support in the evidence introduced in this proceeding.

2. The purported recitals of fact, the findings of fact and the conclusions thereon contained in said order are wholly insufficient to sustain the said order of the Commission and are erroneous, contrary to law and contrary to and without support in the evidence introduced in this proceeding.

3. Said order is erroneous and contrary to law in that it fails to make findings or recitals of fact and conclusions thereon with respect to material, substantial and uncontroverted evidence submitted by the Respondent and received by the Commission.

4. Said order is erroneous and contrary to law in that it contains purported recitals of fact, findings of fact and conclusions thereon which are contrary to the manifest weight of and without any support whatsoever in the evidence received by the Commission.

5. Said order is erroneous and contrary to law in that the purported recitals of fact, findings of

fact and conclusions thereon made by the Commission express mere conclusions not based upon any facts found by it and are not a sufficient basis for said order of the Commission.

6. Said order is erroneous and contrary to law in that in purporting to determine a fair value rate base no allowance whatsoever was made for any value for the physical plant and property of Respondent, which the Commission found to have a total net original cost of $788,610.52 and a reproduction cost new less depreciation of $888,214.04.

7. Said order is erroneous, contrary to law and contrary to the evidence received by the Commission in the proceeding in that in purporting to determine the fair present value of Respondent's utility plant for rate-base purposes, it failed to give any consideration or weight to the reproduction cost new or reproduction cost less depreciation of Respondent's utility plant, as required by law of Illinois and the Constitutions of the State of Illinois and the United States of America.

8. Said order is erroneous, contrary to law and contrary to the evidence received by the Commission in the proceeding in that it failed to make any finding of fact (or recital of fact adopted as a finding of fact) as to the fair present value of Respondent's utility plant, after a full and proper consideration of all the factors of rate-base valuation, including original cost of construction, reproduction cost new, working capital requirements, operating expenses, depreciation, reserves necessary in good business judgment and operations, a reasonable return to the investor on the basis of the present fair value of the property, and a reasonable return sufficient to assure the financial integrity of the Company, maintain its credit and to attract new

capital, as required by the law of Illinois and the Constitutions of the State of Illinois and the United States of America.

9. Said order is erroneous, contrary to law and contrary to the evidence received by the Commission in the proceeding in that in determining the present fair value of Respondent's utility plant for rate-making purposes it failed to give any weight to the original cost of construction of such utility plant.

10. Said order is erroneous, contrary to law and contrary to the evidence received by the Commission in the proceeding in that it deducted the amount of $798,702.25 from its finding of weighted value of net utility plant in service in determining purported fair value rate base.

11. Said order is erroneous and contrary to law in that the Commission in Finding (8) stated that its finding of "contributions in aid of construction" in the amount of $798,702.25 should be deducted from the *cost* of utility plant in service; whereas in Appendix A to said order, the Commission actually deducted so-called "contributions in aid of construction" from the "fair value" of net utility plant in service, a figure comprising and including a 75% weighting to net original cost and 25% weighting to reproduction cost new; the Commission in its recitals of fact at page 11, finds that the Commission's own witness proposed only that said amount be deducted from the *original cost* of the Company for rate base determination, resulting in a zero or negative *original cost component* of rate base, but no adjustment of the *reproduction cost component* of rate base.

12. Said order is erroneous, contrary to law and contrary to the evidence received by the Commission in the proceeding in that it purports to make any

deductions of so-called "contributions in aid of construction" from either original cost, reproduction cost new, or fair value of utility plant in service in determining a fair value rate base.

13. Said order is erroneous, contrary to law and contrary to the evidence received by the Commission in the proceeding in that it found officers' salaries to be excessive and reduced the same by one-half for rate-making purposes.

14. Said order is erroneous and contrary to law in Finding (11) that Respondent's proforma revenue requirements are in the sum of $109,240.00 in that such finding is entirely contrary to and without support in the evidence adduced by the Commission.

15. Said order is erroneous, contrary to law and contrary to the evidence received by the Commission in the proceeding in that it fails to allow Respondent sufficient revenues to cover operating expenses and fails to allow Respondent a just and reasonable return.

16. Said order is erroneous, contrary to law and contrary to and without support in the evidence introduced in the proceeding in that it contains the following findings of fact:

"(7) the salaries of the officers in the sum of $31,680 was excessive and that a more reasonable amount for officers' salaries for the service performed would be 1/2 that amount or the sum of $15,840; that with the adjustment of officers' salaries the working capital requirements of the Respondent as adjusted upon rehearing is $16,555.00 for seventy-five (75) days;

"(8) the sum of $793,195.25 representing cash contributions from interests affiliated with the shareholders of Respondent constitutes 'contributions in aid of construction' and not capital surplus,

and that said sum together with additional contributions in aid of construction in the aggregate amount of $798,702.25 should be deducted from the cost of utility plant in service in computing its fair value for rate making purposes;

"(9) for the purpose of this proceeding, the Company's fair value rate base was no greater than about $16,555;

"(11) Respondent's pro forma revenue requirements as per its Revised Exhibit 8 and adjusted by the addition of the fluoridation expense and certain tax adjustments, less that portion of the officers' salaries disallowed and Federal Income Tax therefor as adjusted, total about $109,240; the 1966 revenues are about $95,511, reflecting a need for an increase of about $13,729 to provide operating revenues sufficient to cover operating expenses and return on fair value rate base, all as set forth in Appendix B attached hereto and made a part of this order;

"(13) the rates proposed by the Du Page Utility Company in this proceeding are unjust and unreasonable, and would yield an excessive return, and should be modified as hereinafter set forth;

"(14) the rates set forth in Appendix C attached hereto and made a part of this Order are just and reasonable, and should be placed in effect as the legal rates for water and sewer service furnished by Du Page Utility Company; said rates are also designed to bring the rates for sewer service in balance with those for water service so far as the general financial condition of the Company is concerned;

"(15) the rates set forth in Appendix C should become effective for current unbilled service on five (5) days' notice."

17. Said order is erroneous, contrary to law and contrary to the evidence received by the Commission in the proceeding in that it contains and refers to Appendix A, Appendix B and Appendix C attached thereto and the matter contained therein.

18. Said order is erroneous and contrary to law and the evidence in that it found unreasonable and disallowed the rate schedule for water service designated Ill. C.C. No. 1, First Revised Sheet No. 1, and the rate schedule for sewer service designated Ill. C.C. No. 2, Third Revised Sheet No. 1, filed by Respondent on February 20, 1967, for water service and sewer service, and it ordered that Respondent file and place into effect the rates for water and sewer service set forth in Appendix C of said order.

19. Said order is erroneous, contrary to law and contrary to and without support in the evidence received by the Commission in these proceedings in that it failed to contain the following finding or recital of fact (adopted as a finding of fact):

FAIR VALUE

The Commission has reviewed the elements of a fair value rate base of the Company as submitted in evidence. It is the duty and prerogative of the Commission to determine a fair value rate base after giving full and proper consideration to the Company's evidence as to original cost, reproduction cost, a proper allowance for depreciation, cash working capital requirements and to all other elements of value which have been shown by the evidence in the case relating to value. On the basis of the evidence received in evidence herein, the Commission finds that the fair value of the Company's property used and useful in rendering water service and sewer-

age disposal service to the public for rate-making purposes is not less than $840,000. The Commission further finds that the fair value of the Company's property used and useful in rendering water service is not less than $510,000, and that the fair value of the Company's property used and useful in rendering sewerage disposal service is not less than $330,000.

OPERATING REVENUES AND DEDUCTIONS

A witness for the Accounting Staff of the Commission proposed that the pro forma operating income of the Company be adjusted by disallowing for rate-making purposes one-half of the annual Officers' salaries. Such adjustment would increase pro forma operating income by $15,840.00 to $42,396.00. He stated that he reviewed the salaries paid to Officers of the Company in light of salaries paid to officers of other companies under the Commission's jurisdiction. However, he stated that the determination of annual Officers' salaries of a corporation is primarily the function of its Board of Directors. He also stated that he is familiar with salaries paid full-time management officials of public utilities generally and that in many cases those salaries exceed the individual amounts paid each of Respondent's Officers. In his opinion, $10,500 was not excessive for an officer who devotes one-half of his normal work week to the affairs of a utility company. The Company's three Officers each testified as to the nature and extent of work they respectively performed for the Company. Each stated that he devotes a substantial amount of his time to the management and operation of the Company, including attendance of directors' meetings, attendance at the Company's

office, handling of complaints, bills, service extensions, maintenance and repairs, preparation and analysis of financial data, etc. The Commission accepts the Company's figures for Officers' salaries because the evidence in the record does not show that the Officers' salaries are unreasonably disproportionate to the nature and extent of work performed by the Officers on behalf of the Company.

20. Said order is erroneous, contrary to law and without support in the evidence received by the Commission in these proceedings in that it failed to contain the following findings of fact:

"(8) that a reasonable allowance to the Company for cash working capital is $19,592.12, comprising $11,007.12 with respect to water service operations and $8,585.00 with respect to sewerage disposal service operations;

"(9) that the indicated fair value for rate-making purposes, as at December 31, 1966, of the total plant and property of Du Page Utility Company is not less than $840,000 after consideration of all elements of value, both tangible and intangible; that the fair value of the Company's plant and property used and useful in providing water service is not less than $510,000; and that the fair value of the Company's plant and property used and useful in providing sewerage disposal service is not less than $330,000;

"(11) that the schedule of rates, Ill. C.C. No. 2, 3rd Revised Sheet No. 1, applicable to sewerage disposal service and Ill. C.C. No. 1, 1st Revised Sheet No. 1, applicable to water service, filed herein on February 20, 1967,

would produce gross operating revenues of $155,557.00 per annum on the basis of the usage of water by customers for the 12 months ended December 31, 1966; the operating expenses including depreciation and Federal Income Taxes would amount to approximately $130,788.00 and the difference between said gross operating revenues and said operating expenses would result in net utility operating income of approximately $24,769.00, which said amount would constitute a rate of return of approximately 2.9% of the aforesaid fair value of the plant and property of Du Page Utility Company above set forth; with respect to water service, there would result gross operating revenues of $102,073.00, operating expenses of $78,732.00 and net operating income of $23,341.00, constituting a rate of return of approximately 4.6% of the aforesaid fair value of plant and property used and useful in providing water service. With respect to sewerage disposal service, there would result gross operating revenues of $53,484.00, operating expenses of $52,056.00, and net operating income of $1,428.00, constituting a rate of return of 0.4% of the aforesaid fair value of plant and property used and useful in providing sewerage disposal service;

"(12) that the rate schedule Ill. C.C. No. 2, 3rd Revised Sheet No. 1, applicable to sewerage disposal service and rate schedule Ill. C.C. No. 1, 1st Revised Sheet No. 1, applicable to water service, filed by Du Page Utility

Company on February 20, 1967, are just and reasonable and should be permitted to become effective immediately."

21. Said order is erroneous, contrary to law, contrary to previous orders of the Commission and contrary to and without support in the evidence received by the Commission in these proceedings in that it failed to order and direct that the rates for water service and sewer service filed by Respondent on February 20, 1967 designated as Ill. C.C. No. 1, 1st Revised Sheet No. 1, applicable to water service, and as Ill. C.C. No. 2, Third Revised Sheet No. 1, applicable to sewer service, should remain effective for all service rendered after the entry of said order.

22. Said order will prevent the Company from charging and receiving just compensation for the use of its property and constitutes the taking of the property of the Company without due process of law and such order is, therefore, confiscatory in nature and effect, in consequence of which it constitutes a violation of Sections 2 and 13 of Article II of the Constitution of the State of Illinois and, also, constitutes a violation of Article XIV, Section 1 of the Articles in addition to and amendment of the Constitution of the United States of America.

23. The proceedings and action on the part of the Commission in failing to fix, determine and prescribe the rates for water service in Ill. C.C. No. 1, First Revised Sheet No. 1, and the rates for sewer service proposed by Respondent in Ill. C.C. No. 2, Third Revised Sheet No. 1, filed herein on February 20, 1967, will prevent Respondent from

charging and receiving just compensation for the use of its property and constitute a taking of the property without due process of law and are, therefore, confiscatory in nature and effect, in consequence of which they constitute a violation of Sections 2 and 13 of Article II of the Constitution of the State of Illinois and, also, constitute a violation of Article XIV of Section 1 of the Articles in addition to and amendment of the Constitution of the United States of America.

24. The proceedings and action on the part of the Commission in failing to fix just and reasonable rates upon the fair value of Respondent's property used and useful in rendering service to the public in its order will prevent Respondent from charging and receiving just compensation for the use of its property and constitutes a taking of the property of the Company without due process of law and are, therefore, confiscatory in nature and effect, in consequence of which they constitute a violation of Sections 2 and 13 of Article II of the Constitution of the State of Illinois and, also, constitute a violation of Article XIV of Section 1 of the Articles in addition to and amendment of the Constitution of the United States of America.

WHEREFORE, the Company prays that the Commission grant it a further rehearing in the above entitled cause to the end that the errors above set forth may be corrected and that the schedules of rates filed by the Company on February 20, 1967 be made effective for all bills rendered for water service and for sewer service, thus affording the Company a sufficient amount available for return after proper expenses to more nearly provide that

reasonable return upon the present fair value of its plant and property used and useful in rendering service to the public as guaranteed by the Constitutions of the State of Illinois and of the United States of America and as prescribed by the Illinois Public Utilities Act.

Opinion by WILLIAM L. GUILD, Associate Judge of the Circuit Court of the 18th Judicial Circuit.

February 6, 1970

Re: MEADOWS COMMUNITY ASSOCIATION and THE OAK VIEW HOMEOWNERS ASSOCIATION vs. ILLINOIS COMMERCE COMMISSION DU PAGE UTILITY COMPANY vs. ILLINOIS COMMERCE COMMISSION	Cases No. 68-1092 G and 68-1511 G

Gentlemen:

This matter appears before me upon a consolidation of the above entitled cases, one is an appeal by the rate payers from the order of the Illinois Commerce Commission entered April, 1967 (68-1092). The Du Page Utility Company has likewise appealed from the orders of the Illinois Commerce Commission of April 16, 1968 and May 29, 1968, and as indicated above the two cases have been consolidated.

The Du Page Utility Company is a public utility furnishing water and sewer facilities, serving the Oakview, Meadows and Four Lakes areas. They have approximately 800 customers and the utility maintains its' office in Lisle. The sewer facilities of the Du Page Utility Company were sold to the County of Du Page sometime back.

In 1967 the utility company filed a proposed rate schedule with the Illinois Commerce Commission seeking a 80

to 100% increase in rates, contending that they were losing money. At the outset, the Commerce Commission found that the fair value of the utility plant, for the rate basis, was zero. However, the Commerce Commission found that the working capital requirements for two and a half months were $16,555.00. The Commerce Commission allows a 6½% return on this amount, resulting in a net profit of $1,076.00 for the use of the utility plant, with an apparent present value of $888,214.00. The simple method by which the Commerce Commission arrives at this figure, $1,076.00, is by deducting the sum of $798,702.25, which the Commerce Commission held to be "Contributions in Aid of Construction", to this the Commerce Commission added customer's advances for construction in the sum of $15,669.64, unamortized investments credited in the sum of $620.80, making a total of $814,992.19. When this amount, $814,992.19, is deducted from the weighted cost of $813,511.40, we have a negative valuation for the rate basis.

Extensive hearings have been had and the record is most voluminous. As a result of this and the fact that the Circuit Clerk's office lost the file for a period of about seven months, this opinion has been delayed, for which I apologize.

Factually, the Du Page Utility Company was incorporated by three people, Messrs. O. L. Krughoff, President, Jack S. Kepler, Vice President and Treasurer and Howard Clark, Secretary. Apparently these three people contributed $15,000.00 toward the formation of this company. This court is not sure as to where the rest of the money came from, but I will go into that further on in this opinion.

Apparently the above three, Krughoff, Kepler, and Clark, also own and run a separate company known as Oakview Improvement Company. The contracts for the sale of lots by Oakview provided that sewer and water were available on the lots sold. The contracts expressly do not state directly or indirectly that the purchasers of the lots have any interest in the Du Page Utility Company or the facilities of the Du Page Utility Company.

Examination of the record further discloses that a portion of the funds received from the sale of the lots was, in fact, applied to the cost of the construction of the utility plant. It is my impression that the utility plant was constructed prior to the sale of any lots. The utility company treated some of the funds received as "Contributions in Aid of Construction" and showed these funds in that fashion. At a later time they changed this nomenclature to "Capital in Excess of Par Value of Shares". It would thusly appear that the utility company treated these funds in a non-taxable fashion for income tax purposes. For the past five years the utility company reported this amount, $793,195.25, as capital surplus.

Counsel for the intervenors has pointed out that the 1966 income tax return indicates that 91.24% of the utility company's assets were "considered as Contributions to Capital and are treated as having a zero tax basis in accordance with Section 362(C) of the Internal Revenue Code" (Intervenor's Exhibit #1). Section 362(C) of the Internal Revenue Code (Staff Exhibit #1) sets forth the basis for contribution to capital. Counsel for the utility company contends that the utility company has not written off anything for tax purposes and is not attempting to restore to rate basis something it previously expensed.

It can thus be seen that the real question before this court is as to whether or not the Commerce Commission acted properly in holding that the figure of $814,992.19 should be deducted from the fair value of the utility plant for rate basis. It is that simple.

The two most important cases cited by the Attorney General, attorney for the respondent, are *Preston Utilities Corp.* v. *Commerce Commission,* 39 Ill. 2nd 457, and *Killarney Water Co.* v. *Commerce Commission,* 37 Ill. 2nd 345. Briefly the Preston case is as follows:

The Preston Management Company built the sewer and water facilities in question and transferred the title then to Preston Homes. They were subsequently transferred from Preston Homes to Preston Service Co. and finally they were sold to Preston Utilities Corp., which was not affiliated with any of the predecessor companies, for $90,000.00. The order of the Commerce Commission found that the depreciated book value of the utility plant, based upon construction costs, was $369,074.00 and that $281,223.00 was miscellaneous paid-in capital, which resulted in the $90,000.00 approved purchase price. Later the Preston Utility Corp. improved the plant and the Commerce Commission found that the depreciation of the utility property was $436,871.00. The Commerce Commission expressly found that they would make no finding "relative to the existence or amount of Contributions in Aid on Construction". As a matter of interest, the Commission allowed a rate schedule that would result in an operating income of 3.87% or $16,900.00.

A rehearing was had and the Commission found that the total utility plant value was $644,844.00, less accumulated depreciation of $148,473.00, leaving a net utility plant value of $496,371.00. This last amount was held to

be the depreciated construction cost of the plant and the Commission then deducted $281,223.00, making an original cost of $215,147.00. Following this, the Commission held that the fair value for rate making purposes of the facilities of Preston Utilities was $288,000.00.

The appellant contended that the Commission erred in deducting $281,223.00, depreciated construction cost, on the basis that there was no evidence that this figure was "Contributions in Aid of Construction". The courts said that the appellant did treat the cost of construction as the inevitable equivalent of original cost for rate-making purposes. The court then held that the Commission properly excluded from the rate base that part of the construction cost that had been paid by consumers who purchased homes in the utility area.

The court decided this case on the basis that the burden of establishing original cost was upon the utility, not upon the Commission. They held in substance that the utility company failed to prove what was actually spent by the first of these series of companies to devote the utility plant to public service.

The question then arises in the instant case as to whether or not the utility company here has proved what was in fact spent for the reconstruction of this plant, other than "Contributions in Aid of Construction".

In the Killarney Water Company case we find really two cases, on Pistakee and the other Killarney, public utilities in McHenry County. The court said that the controversy in these two cases is as to the proper treatment of funds which were segregated by the builders from the amounts it collected from purchasers of lots, and placed in "water reserve" accounts. In other words, should these funds be treated as "Contributions in Aid

of Construction" or as "Donations from Stockholders" within the meaning of the Uniform System of Accounts for water utilities prescribed by the Commission.

In Pistakee the utility did almost the same as in the instant case, it originally recorded these accounts as "Contributions in Aid of Construction". In 1961 they reclassified some $50,000.00 from "Contributions in Aid of Construction" to "Accounts Payable to Shareholders". Later they reclassified this to "*Donations* Received from Shareholders" and contend that these funds should not be treated as "Contributions in Aid of Construction".

In Killarney the builders put $200.00 or $250.00 a lot into a "water reserve" account. These funds were not treated as income by the builders for tax purposes. The court then held or said that the significance of the way the parties to the transaction treated it for tax purposes, as indicating their intention, is pointed out in *Hammer* v. *Sanders*, 8 Ill. 2d 414. In substance the court in this case held that while the factual situation was somewhat different from the instant case, that the treatment by the utility of funds as "Contributions in Aid of Construction" for tax purposes is determinative to some degree of the actual category that the funds find themselves in.

In the case before me there is no question but that the utility treated these funds as "Contributions in Aid of Construction" and I am sure this was done for tax purposes. Reading between the lines it would appear to this court that this was done for capital gain purposes.

While it is true that the paper value of the utility is over $800,000.00, it is obvious that it does not have this value on the open market. I cannot help but feel that the amount of return allowed is, in fact, so small that it probably is not financially feasible for the utility company to

continue operations. I am inclined to agree with the dissent of the late Ralph Dolph, one of the members of the Commerce Commission. However, I am bound by the Supreme Court decisions and I feel that the cases cited specifically apply to the factual situation here.

Insofar as the intervenors are concerned, I feel that their contentions are without merit. I find that the proposed rate schedule is, in fact, lower than most comparable utilities in this area. I think they have a bargain and apparently they do not know it.

The finding of the Commerce Commission will be affirmed; an order may be presented to that effect.

IN THE EIGHTEENTH JUDICIAL CIRCUIT, DU PAGE County, Wheaton, Illinois

MEADOWS COMMUNITY ASSOCIATION and THE OAK VIEW HOMEOWNERS ASSOCIATION, Appellant, vs. ILLINOIS COMMERCE COMMISSION, Appellee.	Cases No. 68-1092 G and 68-1511 G Consolidated
DU PAGE UTILITY COMPANY, Appellant, vs. ILLINOIS COMMERCE COMMISSION, Appellee.	

ORDER

This Court having considered the briefs and oral arguments of the Appellant, Meadows Community Association and The Oak View Homeowners Association, Appellant, Du Page Utility Company, and the Appellee, Illinois Commerce Commission, and being fully advised in the premises:

It Is Hereby Ordered And Decreed that the orders of the Illinois Commerce Commission are hereby affirmed.

Enter:

/s/ William L. Guild

February 24, 1970

Opinion Of The Supreme Court Of Illinois

Docket No. 43137—Agenda 11—November, 1970.
Du Page Utility Company, Appellant, *vs.* Illinois Commerce Commission, Appellee.—(Meadows Community Association *et al.*, Separate Appellants.)

Per curiam: This appeal arises from an order on utility rates entered by the Illinois Commerce Commission, affirmed by the circuit court of Du Page County, and is prosecuted directly to this court pursuant to Rule 302. 43 Ill.2d R. 302.

Du Page Utility Company (Du Page), provides water and sewage disposal service to approximately 840 customers, most of whom are residents of Oak View and Meadows subdivisions located in and near the village of Lisle. On February 20, 1967, Du Page filed with the Commission a new schedule proposing an increase in rates for both services, and was met with the opposition of the Oak View Home Owners Association and the Meadows Community Association, to whom the Commission granted leave to intervene in the cause. After several hearings the Commission entered an order which granted an increase in rates, but not to the extent that had been sought. Both Du Page and the intervenors applied for a rehearing, which was granted, and on April 16, 1968, the Commission entered a second order, being the one involved in this appeal. With the exception of adjustments to reflect the cost of water fluoridation, evidence of which was offered and received for the first time on rehearing, the second order was substantially the same as the first. Du Page also filed an application for rehearing in respect to the second order, which was denied, but the intervenors did not so apply. Thereafter, on separate appeals by Du Page and the intervenors to the circuit court, the order of the Commission was affirmed, and it is the same parties who have appealed to this court. Broadly speaking, it is the contention of Du Page that the Commission made improper deductions from its rate base, whereas it is contended by the intervenors that still further deductions should have been made.

We are met at the outset with a contention of Du Page that the appeal of the intervenors is improper and should be dismissed, its theory being that the failure of the intervenors to apply for a rehearing in respect to the second order caused the circuit court to lack jurisdiction to entertain the intervenors intermediate appeal. (See: Ill. Rev.

Stat. 1967, ch. 111⅔, pars. 71 & 72; *Scherer Freight Lines, Inc.* v. *Commerce Com.*, 24 Ill.2d 359; *Alton Railroad Co.* v. *Commerce Com.*, 407 Ill. 202.) The court below denied a joint motion of the Commission and Du Page seeking dismissal of the intervenor's appeal on the same ground and, we find, correctly so. Where an order of the Commission entered on rehearing is substantially the same as the order being reconsidered, and makes only minor revisions, a second application for rehearing is not required. (*Continental Air Transport Co.* v. *Commerce Com.*, 38 Ill.2d 563; see also, *Central Illinois Light Co.* v. *Illinois Commerce Com.*, Docket No. 43013.) Here, even though evidence of the cost of fluoridation was heard for the first time on rehearing, it resulted only in minor revisions and did not alter the basic issues between the parties, and the two orders were substantially the same.

There is, for the most part, no dispute as to the law which controls in rate cases of this nature, but controversy arises as to its application to the facts of this case. Our law contemplates that utility rates will be just and reasonable and fixed so as to produce a reasonable return on the property used and employed in the public service. To this end we held in *Illinois Bell Telephone Co.* v. *Commerce Com.*, 414 Ill. 275, 286, that the rates fixed by the Commission "* * * should be sufficient to provide for operating expenses, depreciation, reserves that are necessary in good business judgment and operations and a reasonable return to the investor on the basis of the fair value of the utility property." And in the ascertainment of the "fair value" of such property, it has been consistently stated that "* * * the original cost of construction, the amount expended in permanent improvements, the present cost of construction, the probable earning capacity of the property under the particular rates prescribed by statute, and the sum required to meet operating expenses, are all matters for consideration and are to be given such weight as may be just and right in each case." (*State Public Utilities Com. ex rel. City of Springfield* v. *Springfield Gas and Electric Co.*, 291 Ill. 209, 219; *Peoples Gas Light and Coke Co.* v. *Slattery*, 373 Ill. 31; *Illinois Bell Telephone Co.* v. *Commerce Com.*, 414 Ill. 275.) More recently in *Killarney Water Co.* v. *Commerce Com.*, 37 Ill.2d 345, where the facts disclosed that a water company had in effect been built with funds furnished by purchasers of the lots serviced by the utility, we held that the concept of plant fair value for rate-fixing purposes does not include contributions in aid of construction made by the consumers of the utility's service, since it would be unfair

to require such consumers to pay rates based upon the value of a facility for which they have themselves already paid. (See also: *Preston Utilities Corp.* v. *Commerce Com.*, 39 Ill.2d 457; *Westwood Lake, Inc.* v. *Metropolitan Dade County Water and Sewer Board* (Fla.), 203 So. 2d 363; *Mississippi Public Service Com.* v. *Hinds County Water Co.* (Miss.), 195 So. 2d 71.) And, conversely, where consumers have borne the cost of a utility plant, the utility stockholders should not be permitted to recover a return on money that they have not invested.

Following the guidelines of the foregoing decisions, and based upon the evidence before it, the Commission, after making allowances for depreciation, found the original cost of the Du Page plant to be $788,610.52 and reproduction cost new to be $888,214.04. And after applying weighting factors to each figure, about which factors there is no dispute, the fair value of the plant was found to be $813,214.04. From the latter figure, however, the Commission deducted a total of $814,922.19, and thus arrived at a plant fair value of zero for rate-making purposes. Included in the sum deducted were the following: (1) $798,702.25 deemed by the Commission to have been contributions in aid of construction; (2) $15,669.64 representing customer advances for construction; and (3) an unamortized investment credit of $620.30. We find in *Du Page's* brief no argument or authority concerning the last item, and thus we need consider only its contentions that the first two items were improperly deducted. Looking first and principally to the item of $798,702.25, Du Page insists that it does not represent contributions in aid of construction, but is in fact cash donations to capital made by a corporate affiliate, and contends that our decision in *Killarney* does not stand as authority for its deduction from the rate base.

Facts gathered from the record disclose that Du Page has three shareholders, each of whom initially invested $5,000 for 50 shares of capital stock, respectively, which represents all of the issued and outstanding stock in the utility. There is no evidence that any of them personally invested further funds or made contributions to capital. Each is also an officer and director of Du Page, and each has been paid an annual salary of approximately $10,553 for their services as officers. The same three men were originally partners and subsequently equal shareholders in Oak View Improvement Company, (hereinafter referred to as the development company), a corporation engaged in

the development of the real estate serviced and to be serviced by Du Page. The development company sold both improved and unimproved lots in the Meadows and Oak View subdivisions, and prospective purchasers were informed that all improvements, including sewer and water, were included in the price of the lots. A form of contract introduced into evidence provided that all improvements, including sewer and water, were in and fully paid for and that no assessments would be levied therefor.

Funds from the sale of the lots were deposited in a bank account of the development company and, from time to time, some of such funds were subsequently transferred to Du Page. In the books of the latter these funds were carried in a ledger account designated as "Contributions in Aid of Construction" and, as of September, 1966, there was a closing balance of $739,195.25 in such account. But on December 31, 1966, Du Page changed the designation of the account to "Capital in Excess of Par Value of Shares." This change, we observe, took place but seven weeks before the initiation of the instant proceeding to increase rates and, as disclosed by the records of this court, subsequent to the orders of the Commission later affirmed by this court in the *Killarney* case. (37 Ill.2d 345.) Further, certified copies of annual corporate reports, filed by Du Page with the Secretary of State and introduced in evidence by the intervenors, reflected that during the years 1962 through 1967, inclusive, Du Page reported no paid-in surplus and showed as its sole capital $15,000 of stated capital. The Commission found that the funds transferred by the development company to Du Page were rightly contributions in aid of construction, rather than capital surplus, and found that such funds had been used by Du Page to build its utility plant. While not so stated in express terms, it is the thrust of Du Page's arguments that these findings are against the manifest weight of the evidence.

To support its contention that the consumers, or lot purchasers, had contributed nothing to the construction of the utility plant, Du Page represents the record as establishing two things. First, that Du Page itself purchased, paid for and installed all of its utility plant with its own funds prior to the sale of lots; and, second, that the cost of plant was not charged to, or allocated to, or paid by the lot purchasers. But we do not find clear or convincing proof for either proposition. Just when the utility plant was completed in relation to the beginning of the sale of lots does not ap-

pear, and we note that Du Page's president testified: "I cannot tell you the exact date that it was started. * * * The sewage plant, and the water plant developed at the same time and along with the development of the Oak View Subdivision and the Meadows Subdivision." The same witness did indeed testify that the cost of the utility had not been amortized by the development company over the purchase price of the lots, and further stated that Du Page had not incurred any indebtedness with reference to the construction of sewer and water facilities, but had paid for "everything" with funds supplied by "the stockholders and affiliated people." Also, on cross-examination, however, he was forced to concede that in a 1963 proceeding before the Commission involving Du Page, an accountant then employed by the utility had testified that the funds received from the sale of the lots were treated as assets of the development company, that the expense of developing the sewer and water systems was carried as an element of the cost of the land, and that the funds transferred to Du Page were considered as development costs and prorated over the lots to be sold and expensed to those units as they were sold. In addition, it appears from his testimony that the developer charged off the funds transferred to Du Page as expenses for income tax purposes and thus arrived at a zero tax basis for such funds. And in connection with the contention that the utility was fully installed and paid with Du Page's own funds prior to the time lots were sold, we note the accountant also testified in the prior proceeding that the development company had made "advances or donations" to Du Page for the construction of water mains and underground water facilities.

Nor can we agree, as further claimed by Du Page, that the testimony of its accountant who testified in the present proceeding establishes that Du Page paid for its plant with its own funds. When testifying in regard to the utility's books the witness said he assumed that the original cost of plant was $875,418.55 and that Du Page had obtained cash and "spent the cash for the plant." But when specifically asked if he meant the cash had been furnished by Du Page, he stated: "I didn't say that. I said it was plant purchased by Du Page over a period of years. * * * cash came from various sources, part from operation. It came from donations as you mentioned."

The legislature has made the fixing of utility rates an exclusive function of the Commission, and although a court may hold that rates authorized by the Commission are in-

adequate or illegal and restrain their enforcement, it cannot make new rates. (*Peoples Gas Light and Coke Co.* v. *Slattery*, 373 Ill. 31; *South Chicago Coal and Dock Co.* v. *Commerce Com.*, 365 Ill. 218.) Orders of the Commission "are entitled to great weight and when the sufficiency of an order is questioned it will not be set aside unless it is clearly against the manifest weight of the evidence, is arbitrary or unreasonable, or in clear violation of a rule of law." (*Illinois Bell Telephone Co.* v. *Commerce Com.*, 414 Ill. 275, 289-290.) We find no such deficiency in the order here being reviewed. Despite the claims of Du Page, the weight of the evidence, including its own record treatment of the funds involved, clearly establishes that the utility plant was, in fact, paid for by the lot purchasers in the two subdivisions, and that the amount so contributed by the purchasers should, consistent with *Killarney*, be excluded from the rate base.

The situation here is little different from that in the case of *Re Green-Fields Water Co.*, (N.J. 1964) 53 PUR 3d 670, another case where there was an attempt by a utility to reinstate to rate base the cost of a part of the utility previously written off for tax purposes as land development costs, and with which we are in accord. In that case, water mains having a cost of about $150,000 were installed by two development companies which paid the installation costs, charged off the costs for income tax purposes, and offset the costs against sales prices of homes, after which the mains then had a zero tax basis to the development companies. Thereafter, the development companies, whose principal shareholders owned one half of the securities of the company, conveyed and transferred the mains to the utility in consideration of 1500 shares of stock having a par value of $100 per share. On the basis of such facts the New Jersey Public Utilities Commission found and concluded as follows: "It also appears that the developers in the area turned over the entire distribution facilities required to furnish water service to their housing developments and that these facilities were paid for by such developers and the expenses thereof were fully recovered for income tax purposes so that the value of these facilities to the transferors was carried at a zero basis.

" 'In view of these conclusions it is the board's opinion that $150,000 of utility plant representing the distribution system facilities was, in fact, paid for by the homeowners in the developments and contributed to the petitioner. Under

these circumstances the board is of the opinion that the computation of rate base for purposes of this proceeding should be reduced by $150,000.' " In the case presently before us it is true that Du Page, rather than the development company, actually constructed the plant, but this is a distinction without a difference. In both cases the facilities were, in fact, paid for by the lot purchasers in the housing developments, and the cost of the facilities written off for tax purposes as land development costs. Accordingly, we hold that the Commission properly held that the $798,702.25 was contributions in aid of construction, and properly deducted it from the rate base.

Without citation of authority or convincing argument, Du Page next contends that even if it be conceded that the funds transferred to it by the development company were contributions in aid of construction, they should have been deducted only from the original cost of the plant or, alternatively, only from the net cost of the plant, *i.e.*, gross original cost and reproduction new, before depreciation. But to adopt either theory would require the consumers to in part pay again for facilities for which they have already paid in full, contrary to our decision in *Killarney*.

It is next urged that the Commission improperly deducted the sum of $15,669.64, representing customer advances for construction, for the reason that there is a possibility that some or all of such advances may be refunded entirely. We think it sufficient to say that until such refunds in fact occur, the Commission could properly treat this item as further contributions in aid of construction and properly deduct it from the plant fair value as it did.

The Commission also found that the annual salaries of the three officers, a total of $31,680, were excessive and out of proportion to the extent and nature of the services performed and, for rate purposes, disallowed one half thereof, or $15,840, as an operating expense. Du Page's contention that this was an arbitrary action of the Commission, and totally without support in the record, borders on the facetious. The uncontradicted testimony of the officers themselves established that none had previous experience in managing a utility, that they worked only part time and that they had maintained only a minimal contact with day-to-day operations. None could produce records of time spent at the utility business, none maintained an office there and each was active as president of one of three different construction firms. Further, a witness for the Commission testified

that he had reviewed the salaries in light of those paid by other companies under the Commission's jurisdiction and stated that he had found no instance where a utility servicing but 840 customers paid its officers salaries of such magnitude. Nor is Du Page aided by *Village of Milford* v. *Commerce Com.*, 20 Ill.2d 556, where it was held that total salaries of $62,400 for the three officers of a telephone company was not unreasonable or excessive. In that case the officers worked full time, one of them even performing the company's legal services without charge, and the addition of modern equipment increased the scope and complexity of their duties. There are few, if any, parallels in the instant case. Based upon the record, the Commission was correct in its finding that the larger salaries were not justified.

In regard to this deduction, the intervenors go even farther and contend that the Commission should not have allowed any of the officer's salaries in the determination of the rate base, their position being that the officers performed no services of value to the utility causing the payments to them to amount to no more than a distribution of profits. To agree to such a contention would produce a result that is arbitrary and against the manifest weight of the evidence. The testimony of the officers that they performed part time services for the company and the extent of those services was uncontradicted, and there was no proof, nor do we find, that the services were without value to the company.

The Commission also allowed as an operating expense the sum of $15,000, to be amortized at the rate of $3,000 annually, for rate-case expense, and it is the contention of the intervenors that this allowance was improper. While a matter of first impression in this court, we find that rate-case expense is ordinarily properly and fairly allowed as an operating expense. See: *Streator Aqueduct Co.* v. *Smith* (Dist. Ct. S.D. Ill. 1923), 295 Fed. 385, 391; *Westwood Lake* v. *Metropolitan Dade County Water and Sewer Board* (Fla.), 203 So. 2d 363, 366; *West Ohio Gas Co.* v. *Public Utilities Com. of Ohio* (1934), 264 U.S. 63, 79 L. Ed. 761; *Scranton-Spring Brook Water Service Co.* v. *Public Service Com.*, 119 Pa. Super. 117, 181 Atl. 77; *Driscoll* v. *Edison Light & Power Co.* (1939), 307 U.S. 104, 83 L. Ed. 1134.

Complaint is also lodged by the intervenors because the Commission allowed Du Page a working capital allowance of $16,555 in the rate base. We find no merit to this contention. Although we believe that the arguments of the intervenors on this point distort the record in respect to the sufficiency of the utility's operating funds and yearly cash balances, it is sufficient to say that the Commission and this court have long approved the addition to rate base of a working capital allowance, in relation to billing periods, to enable a utility to meet current expenses and contingencies which develop in day-to-day operations. See: *State Public Utilities Com.* v. *Springfield Gas Co.*, 291 Ill. 209; *Peoples Gas Light and Coke Co.* v. *Slattery*, 373 Ill. 31.

Finally, the intervenors contend that the Commission, in computing operating expense, improperly allowed Du-Page a depreciation rate of approximately 1.6% of the depreciable plant. The propriety of allowing a reasonable depreciation deduction on the property of a utility is not dependent upon the source of funds for the original construction of the facility. (*Cf. Langan* v. *West Keansburg Water Co.*, 51 N.J. Super. 41, 143 A. 2d 185.) Du Page will be required to replace from time to time properties which have become obsolete or whose useful lives have expired, in order to sustain service to its customers. This being the case, Du-Page is entitled to a reasonable depreciation deduction on its entire plant in service for the purpose of computing its operating expenses. Intervenors' contention that current maintenance will continually extend the life of the system begs the question since depreciation by definition includes only that loss which cannot be restored by current maintenance. See *Lindheimer* v. *Illinois Bell Telephone Co.* (1934), 292 U.S. 151, 167, 78 L. Ed. 1182.

The judgment of the circuit court of Du Page County is affirmed.

Judgment affirmed.

IN THE

SUPREME COURT OF ILLINOIS

NOVEMBER TERM, 1970

DU PAGE UTILITY COMPANY,

Appellant,

vs.

ILLINOIS COMMERCE COMMISSION,

Appellee.

Appeal from Circuit Court for the
Eighteenth Judicial Circuit, Du Page County.
Trial Court Nos.
68-1092-G and 68-1511-G
Consolidated
Honorable WILLIAM L. GUILD, *Presiding Judge.*

PETITION FOR REHEARING BY APPELLANT DU PAGE UTILITY COMPANY

Appellant Du Page Utility Company respectfully petitions this Court for rehearing with respect to the Per Curiam opinion of this Court, and respectfully suggests that in rendering said opinion this Court overlooked or misapprehended the following points:

I. THE COURT OVERLOOKED THE POINT THAT THE EFFECT OF THE COMMISSION'S ORDER IS TO DEPRIVE DU PAGE OF ALL BENEFITS OF OWNERSHIP YET IMPOSE A DUTY TO MAINTAIN AND OPERATE THE PLANT

With the burden, should come the benefit. The Commission, however, has permitted Du Page only the burden. It has denied Du Page *any return.* Du Page *owns* its plant. It uses this plant to operate a public utility business and to provide public utility service to nearly 1,000 customers. The plant has *value.* It is required to repair, maintain, and improve the plant. It must operate the plant. It must provide service. It cannot cease business or close its doors.

Yet—no return. In no other situation has the law denied a legitimate private enterprise the right to earn a return, yet compelled it to continue to operate. The owner forever is deprived of any and all economic benefit whatsoever from ownership. This *is* confiscation.

Our Constitution and law permit such results nowhere else. For example, a donee of any other property may sell it or rent it for whatever it can bring on the market place. Even upon acquisition by government through eminent domain, he is constitutionally entitled to receive its full market value.

Even conceding for argument that $800,000 should be deducted, what standard does the Commission and Court leave for determining a utility's right to earnings? The legislature said Du Page is entitled to "a *reasonable return* upon the *value* of said public utility's property used and useful in rendering its service to the public." (Emphasis added.) Ill. Rev. Stat., c. 111⅔, sec. 36. This standard has been abandoned by administrative fiat and Court ap-

proval, despite the Court's recognition of the traditional standards by its reference to *Public Utilities Commission* v. *Springfield Gas Co.*, 291 Ill. 209 (1920). What standard, what "right" to the "reasonable return" is substituted for it?

It is stated that the customers paid for Du Page's plant when they purchased their lots. This conclusion is reached primarily because the developer—shareholder "expensed" his donations to Du Page for federal income tax purposes. Application of this "expensing" theory to determination of utility rate base, however, creates a unique phenomenon in the law of property. The immediate result is to deprive the utility of all earnings and to, in effect, transfer the economic ownership of the utility property to the customers, who in turn receive free service to the extent they pay no capital costs.

In arriving at such a result, the Court may not have given consideration to the fact that the homebuilder preparing a complete package for sale also expenses many other items without any similar shift in the economic benefits of property ownership. The homebuilder expenses carpentry, plumbing, electrical and masonry costs for presumably the same tax purpose, but is not required to return to the home purchaser any part of the purchase price equivalent of his so-called tax benefit. He also expenses heavy equipment, automobiles and office buildings, but still retains the full economic benefit of ownership of such items, even though it might be said that he used the home purchasers' money to pay for them if the Court were to "trace" the dollars in the same manner it does where the *developer* invests in water and sewer improvements. Yet, as a result of the Court's initial decision, he is completely deprived of the economic benefit of one class of property only; i.e., his stock in the utility company.

At any rate, what is this "expensing" of costs? It is merely an accountant's bookkeeping entry. The home-builder who received the purchase price from the purchaser may have used the cash in countless different ways; for example, to pay off a bank loan or to buy more land. The mere accounting entry surely does not establish that the money is traceable into the utility plant.

We also point out that if the developer-stockholder did not "expense" his donations to the capital of Du Page, this would not make the donations any more or any less "customers' funds" under the Commission's theory. How is the lack of "expensing" presumptive evidence that customers did not pay for plant under this argument? There is no showing that the price paid by the home purchaser is affected at all by the tax accounting or bookkeeping of the developer. Rather the record is to the contrary in that the sales price is solely based upon the competitive housing market.

The Commission's order, to paraphrase Cardozo, illustrates the tendency of a "principle" to extend beyond the limit of its logic. Does the theory that the customers paid for Du Page's plant when they purchased their lots apply to a second owner of a house—the transferee of the original lot purchaser? Suppose part of the price of a lot were used by the developer to build houses. Are the lot purchasers entitled to a discount on the purchase of houses because they "paid" for them already?

Do the lot purchasers have an interest in the developer's car or his wife's fur coat? If the developer used the funds to purchase stock of Commonwealth Edison—who also put lines in and serves the subdivision—could he properly keep dividends on the stock? Would the lot purchasers be entitled to discounts on their electric bills? If Du Page fi-

nanced its plant with a bank loan, but repaid the loan with these funds donated by the shareholders, would there still be a zero rate base? If customers of Commonwealth Edison buy company bonds and the proceeds are used to build a nuclear generating plant, can Edison earn a return on this plant; or was it "paid" for by customers?

What is left Du Page? A return of $1,076 for a responsibility to almost 1,000 customers and a net plant having a value of over $800,000. Operating expenses approved by the Commission are over $109,000. What if a well fails or a main breaks, at a cost in excess of $1,076? Who will pay for it?

The Court's ruling leaves Du Page on the horns of a dilemma. How can Du Page attract new capital from investors when it is denied a return? Interest is not includable in operating expense. Accordingly, Du Page can never obtain a bank loan or sell equity or debt securities. In effect, then, the only way Du Page *could* finance new plant or plant repair and replacement is by *demanding* contributions! Such result clearly is contrary to the well established law that a utility is entitled to rates sufficient to attract capital from investors. As this Court held in *Utilities Com.* v. *Springfield Gas Co.*, 291 Ill. 209, 219 (1920), "the real test of the justice and reasonableness of of any rate seems to be that it should be as low as possible and yet sufficient to induce the investment of capital in the business and its continuance therein."

If the Court affirms the Commission's order, it leaves Du Page without any reason to be in business yet compelled to stay in business. It reduces Du Page to the equivalent of a receivership or trustee in bankruptcy. This is confiscation.

II. THE COURT OVERLOOKED THE EVIDENCE THAT THE LOT PURCHASERS DID NOT PAY FOR THE UTILITY PLANT

A. IF THERE WERE DONATIONS, THEY WERE FROM SHAREHOLDERS AND THEIR AFFILIATES, NOT FROM CUSTOMERS.

The argument that customers paid for Du Page's plant was first advanced by the Commission on appeal. As a reading of the Commission's order shows, it made *no* finding that the utility plant was built with customers' funds. The only witness for the Commission, an accountant, *never* proposed that the plant was paid for by customers' funds. Instead, he adopted Du Page's position that these were the developer's funds, or affiliates of the shareholders. His testimony, however, was that donations from shareholders' affiliates should be classified under the Commission's account rules (Uniform System of Accounts) as contributions in aid of construction rather than as donations to capital. This was *not* because lot purchasers "paid" for the plant, but because under the System of Accounts, contributions, regardless of source, must be classified into the contributions account, in his view. (See R. Vol. 1, Unit 2, Sec. 35, pp. 301-302)

We believe that the strong emotional argument of the Commission on appeal that customers would be made to pay twice for the plant may have confused the issues and obscured the record, causing the Court to overlook the fact that there is no evidence that plant was paid for by customers' funds. Indeed, a review of the facts cited by the Court in concluding that the lot purchasers paid for the plant disclose consistently that these funds at all times were the developer's funds. As the Court recites, the evidence is that Du Page purchased, paid for and installed all of its utility plant with cash in its own treasury. Apart

from cash received through loans and earnings, these funds were received by the developers, who were owned by the shareholders, or from the shareholders directly. At all times, these funds donated by the developers were considered by the developers as their money. There is no testimony whatsoever to the contrary. Even the former accountant testifying in the 1963 proceeding stated that funds received from the sale of lots were treated as assets of the developer; and that the developer treated all money from the sale of lots as his income for tax purposes. Several witnesses for Du Page repeatedly testified that no part of the cost of the utility was allocated to specific lots. That only $15,000 of stated capital was reported to the Secretary of State is irrelevant because during the same period Du Page reported to the *Commission* in its annual reports that the subject money was donations to capital.

Accordingly, the most that can be said is that a substantial portion of the cash which Du Page used to pay for its plant came to Du Page from developers. However, this certainly does not mean that this cash was customers' cash. Moreover, it certainly does not mean that this amount should be deducted when determining rate base because these developers were owned by Du Page's shareholders. Accordingly, there is no difference between what occurred in this case and a situation whereby instead of causing their development companies to donate capital the shareholders personally took the cash and gave it to Du Page. They were capital funds and there is no distinction in the essence of the funds donated to the capital by the developers and the $15,000 given by the shareholders in exchange for stock. Even if customer contributions may be deducted from rate base, this is no justification for deduction of donations by shareholder affiliates.

B. THE EVIDENCE IS THAT LOT PURCHASERS MADE NO PAYMENTS FOR PLANT

The Court's opinion states that a form of contract introduced into evidence provided that all improvements, including sewer and water, were in and fully paid for, and apparently relies on this fact in concluding that the customers had paid for the plant. However, the language of the Court is consistent with the evidence that the water and sewer improvements were in prior to the sale of the lot and fully paid for prior to the sale of the lot. The prospective purchasers were not informed that water and sewer improvements were included in the price of the lots in the sense that part of the price was allocated to the improvements. Rather, they were informed that for the given price, they would receive a lot fully improved. The purchase price was then paid to the *developer, not to the utility.* The evidence is that the price was not determined by adding in a factor for the improvements but instead was determined by competition and the market place. The utility improvements were made by the *utility, not the developers.*

With respect to the form of contract in evidence, the clear testimony is that all the utility plant to serve that lot had been installed *prior* to the contract and that no part of the purchase price was used for the cost of installation of the utility facilities. (R. Unit II, Vol. 2, Sec. 35, p. 270). What could be more clear than the testimony in the record?

No customer ever gave any money to Du Page, the developer or anyone for the purpose of constructing plant. Plant was built in various stages. (*Id.*, p. 270; p. 335). Indeed, today there remain about 30 unsold lots which are improved. Who paid for the utility facilities in place to serve these unsold lots? The contractual obligation was not to install utility facilities with funds from the contract

price. The obligation, instead, was to have a lot already improved at the time of the closing of the contract.

C. THE EVIDENCE IS THAT THE KILLARNEY DECISION DOES NOT APPLY

The Commission repeatedly in the appeal has attempted to carve this case within the boundaries of the Court's decision in *Killarney Water Company* v. *Commerce Commission,* 37 Ill. 2d 345 (1967). However, nothing could be more clear than the conclusion that *Killarney* does not apply. In *Killarney,* the controlling factor was that the utility plant was built by the developers and builders, not the utility, and that the plant was paid for with money which the developers and builders did not treat as income nor as money belonging to them. The Court's opinion there repeatedly states and emphasizes the fact that neither the builders nor later the utility regarded these funds as belonging to the builders while the plant was being constructed. Moreover, the evidence showed segregated accounts on the books of the builder whereby these funds used to build the utility plant were not included in the account for sales of land but instead were entered in a separate account called a water reserve account. These segregated water reserve funds were never included in the income of the developer for tax purposes.

Clearly, these controlling facts in *Killarney* do not appear in the instant case. Funds from the sales of lots herein were not segregated; they were fully treated by the developers as income, were always treated as their own funds, and were never considered by the developer to be allocated on behalf of any lot purchaser for the construction of utility plant. Unlike in *Killarney,* Du Page and no one else built and paid for its plant. Unlike *Killarney,* no funds were ever placed in reserve accounts, segregated, or ever treated by either Du Page or the developers as cus-

tomers' funds. Unlike *Killarney,* no developer ever considered the money other than his money. Unlike *Killarney,* no part of the cost of plant was passed on to the customers.

D. THE MERE PURCHASE OF AN IMPROVED LOT DOES NOT MEAN THAT THE CUSTOMER HAS MADE A CAPITAL CONTRIBUTION FOR UTILITY PLANT

When the Commission's argument is distilled, we find that the so-called customer contribution is somehow implied from the fact that the customer purchased an improved lot.

In affirming the Commission's order, the Court may have overlooked the decision of the United States Supreme Court in an analogous case, *Board of Public Utility Commissioners* v. *New York Telephone Company,* 271 U.S. 23 (1926). It was argued there that by paying rates for utility service producing revenues in excess of operating expense, customers were paying for the utility plant, and that such plant therefore could not be used to support future rate increases.

The Supreme Court rejected this argument with language which is wholly applicable to the Du Page situation. The Court first noted that "the relation between the company and its customers is not that of partner, agent and principal or trustee and beneficiary." *Id.* at 31. This statement is important because the utility plant of Du Page is plant clearly owned by it, both legally and equitably, it has value, and it is used and useful in rendering public service.

The Supreme Court then held as follows:

> "Customers pay for service, not for the property used to render it. Their payments are not contributions to depreciation or other operating expenses or to capital to the company. By paying bills for service

> they do not acquire any interest, legal or equitable, in the property used for their convenience or in the funds of the company. Property paid for out of moneys received for service belongs to the company just as does that purchased out of proceeds of its bonds and stock." *Id.* at 32.

The lot purchaser in the instant case paid for land and not utility plant, just like customers paid for service and not for plant. The money paid the developers belonged to the developers. The lot purchasers lost all title and interest in the money after payment. They certainly acquired no interest, legal or equitable, in the utility plant. If customer does not make a contribution by paying rates to a utility, he certainly does not make one by buying a lot which is already improved by the utility, not the developer, in advance of the purchase.

Wherefore, Appellant prays that its petition for rehearing be granted; that on rehearing, the Court should conclude that the Commission's order on rehearing is contrary to the law and evidence because it failed to allow rates which provide a reasonable return on present fair value rate base; and that accordingly the Commission's order is void and should be reversed.

Respectfully submitted,

CHAPMAN AND CUTLER
111 West Monroe Street
Chicago, Illinois 60603
RAndolph 6-6130
Attorneys for Appellant

JOHN N. VANDER VRIES
DANIEL J. KUCERA
Of Counsel

ORDER OF THE SUPREME COURT OF ILLINOIS

BE IT REMEMBERED, that, to-wit: on the 31st day of March, A.D. 1971, the same being one of the days of the term of Court aforesaid, the following proceedings were, by said Court, had and entered of record, to-wit:

DuPage Utility Company,
Appellant

No. 43137 vs.

Illinois Commerce Commission, et al.,
Appellees

Appeal from Circuit Court DuPage County

And now, on this day, the Court having duly considered the petition for rehearing filed herein, and being now fully advised of and concerning the premises, doth overrule the prayer of the petition and denies a rehearing in this cause.